1-1-2009

Health care industry developments - 2009; Audit risk alerts

American Institute of Certified Public Accountants

AICPA Member and
Public Information:
www.aicpa.org

AICPA Online Store:
www.cpa2biz.com

0223409

Health Care Industry Developments – 2009

AICPA®

American Institute of Certified Public Accountants

AUDIT RISK ALERT

2009 Health Care Industry Developments

Strengthening Audit Integrity
Safeguarding Financial Reporting

AICPA®

AUDIT RISK ALERT

2009

Health Care Industry Developments

STRENGTHENING AUDIT INTEGRITY
SAFEGUARDING FINANCIAL REPORTING

AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS

AICPA®

1776-341

ACPA108-ARA-HCO-without.indd 1 9/24/09 1:54 PM

1 2 3 4 5 6 7 8 9 0 AAP 0 9

ISBN 978-0-87051-843-0

Notice to Readers

This Audit Risk Alert is intended to provide auditors of financial statements of health care entities with an overview of recent economic, industry, technical, regulatory, and professional developments that may affect the audits and other engagements they perform. This Audit Risk Alert also can be used by an entity's internal management to address areas of audit concern.

This publication is an *other auditing publication*, as defined in AU section 150, *Generally Accepted Auditing Standards* (AICPA, *Professional Standards*, vol. 1). Other auditing publications have no authoritative status; however, they may help the auditor understand and apply the Statements on Auditing Standards.

If an auditor applies the auditing guidance included in an *other auditing publication*, he or she should be satisfied that, in his or her judgment, it is both relevant to the circumstances of the audit and appropriate. The auditing guidance in this document has been reviewed by the AICPA Audit and Attest Standards staff and published by the AICPA and is presumed to be appropriate. This document has not been approved, disapproved, or otherwise acted on by a senior technical committee of the AICPA.

Christopher Cole, CPA, CFF, CFE
Technical Manager
Accounting and Auditing Publications

Acknowledgments

The AICPA staff is grateful to the following individuals for their essential contributions in creating this publication.

Mark Albrecht, CPA
Robert Beard, CPA
Nicole Blythe, CPA
Marci Thomas, CPA

TABLE OF CONTENTS

Paragraph

How This Alert Helps You

.01 This Audit Risk Alert (alert) helps you plan and perform your health care industry audits and also can be used by an entity's internal management to address areas of audit concern. This alert provides information to assist you in achieving a more robust understanding of the business, economic, and regulatory environments in which your clients operate. This alert is an important tool to help you identify the significant risks that may result in the material misstatement of financial statements and delivers information about emerging practice issues and current accounting, auditing, and regulatory developments. You should refer to the full text of accounting and auditing pronouncements as well as the full text of any rules or publications that are discussed in this alert.

.02 Certain accounting guidance referenced in this alert has been codified into the Financial Accounting Standards Board (FASB) *Accounting Standards Codification*™ (ASC). On June 30, 2009, FASB issued FASB Statement No. 168, *The* FASB Accounting Standards Codification™ *and the Hierarchy of Generally Accepted Accounting Principles—a replacement of FASB Statement No. 162*. On the effective date of this statement, FASB ASC became the source of authoritative U.S. accounting and reporting standards for nongovernmental entities, in addition to guidance issued by the Securities and Exchange Commission (SEC). At that time, FASB ASC superseded all then-existing, non-SEC accounting and reporting standards for nongovernmental entities. Once effective, all other nongrandfathered, non-SEC accounting literature not included in FASB ASC became nonauthoritative. See the discussion of FASB ASC in the "Accounting Issues and Developments" section of this alert.

Audit Risk

.03 It is essential that the auditor understand the meaning of audit risk and the interaction of audit risk with the objective of obtaining sufficient appropriate audit evidence. In AU section 312, *Audit Risk and Materiality in Conducting an Audit* (AICPA, *Professional Standards*, vol. 1), *audit risk* is broadly defined as the risk that the auditor may unknowingly fail to appropriately modify his or her opinion on financial statements that are materially misstated. At the account balance, class of transactions, relevant assertion, or disclosure level, audit risk consists of the risks (both inherent risk and control risk) that the relevant assertions related to balances, classes of transactions, or disclosures contain misstatements (whether caused by error or fraud) that could be material to the financial statements when aggregated with misstatements in other relevant assertions related to balances, classes of transactions, or disclosures and the risk (detection risk) that the auditor will not detect such misstatements.

.04 The auditor's combined assessment of inherent risk and control risk is described as the risks of material misstatement. The auditor should use information gathered by performing risk assessment procedures, including the audit evidence obtained in evaluating the design of controls and determining whether they have been implemented as audit evidence to support the risk assessment. The auditor should use the risk assessment to determine the nature, timing, and extent of further audit procedures to be performed.

.05 As set forth in paragraph .12 of AU section 312, the auditor may reduce audit risk by determining overall responses and designing the nature, timing, and extent of further audit procedures. Furthermore, paragraph .19 of AU section 312 explains that the auditor should seek to reduce audit risk at the individual balance, class, or disclosure level in such a way that will enable the auditor to express an opinion on the financial statements as a whole at an appropriately low level of audit risk.

Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement

.06 AU section 314, *Understanding the Entity and Its Environment and Assessing the Risks of Material Misstatement* (AICPA, *Professional Standards*, vol. 1), establishes requirements and provides guidance about implementing the second standard of field work, as follows: "The auditor must obtain a sufficient understanding of the entity and its environment, including its internal control, to assess the risks of material misstatement of the financial statements whether due to error or fraud, and to design the nature, timing, and extent of further audit procedures." Obtaining this understanding is further complicated by the rapidly changing economic environment. In accordance with paragraph .04 of AU section 314, the auditor's primary consideration is whether the understanding that has been obtained is sufficient to assess risks of material misstatement of the financial statements and to design and perform further audit procedures.

.07 The auditor's understanding of the entity and its environment consists of an understanding of the following:

- Industry, regulatory, and other external factors
- Nature of the entity
- Objectives and strategies and the related business risks that may result in a material misstatement of the financial statements
- Measurement and review of the entity's financial performance
- Internal control, which includes the selection and application of accounting policies

.08 Appendix A of AU section 314 contains examples of matters that the auditor may consider in obtaining an understanding of the entity and its environment relating to the categories previously discussed. Understanding the effects of the current economic climate on each specific audit client is a key step in designing the audit plan.

.09 Business risks result from conditions, events, circumstances, actions, or inactions that could adversely affect the entity's ability to achieve its objectives and execute its strategies. The setting of inappropriate objectives and strategies also results in business risks. Just as the external environment changes, the handling of the entity's business also is dynamic, and the entity's strategies and objectives change over time. An understanding of business risks increases the likelihood of identifying risks of material misstatement; however, the auditor does not have a responsibility to identify or assess all business risks. Most business risks will eventually have financial consequences and, therefore, an effect on the financial statements; however, not all business risks give rise to risks of material misstatement.

.10 Additionally, health care entities may be subject to specific risks of material misstatement arising from the nature of the business, the degree of regulation, or other external forces (for example, political, economic, social, technical, and competitive forces). After obtaining a sufficient understanding of the entity and its environment, including its internal control, an auditor should identify and assess the risks of material misstatement at the financial statement level and at the relevant assertion level related to classes of transactions, account balances, and disclosures based on that understanding. Understanding and properly addressing, as necessary, the matters presented in this alert will help you gain a better understanding of your client's environment, better assess risks of material misstatement of the financial statements, and strengthen the integrity of your audits.

Economic and Industry Developments

The Current Economic Crisis

.11 When planning and performing audit engagements, an auditor should understand the economic conditions facing the industry in which the client operates. Economic activities relating to factors such as interest rates, availability of credit, consumer confidence, overall economic expansion or contraction, inflation, and labor market conditions are likely to have an effect on an entity's financial statements.

.12 Currently, the U.S. economy continues to experience severe instability. The National Bureau of Economic Research officially declared that, as of December 2007, the United States slid into a recession. The length and severity of the economic downturn are yet to be determined. Some key occurrences that exhibit the gravity of the economic crisis include the following:

- U.S. real gross domestic product (GDP), the broadest measure of economic activity, continues to decrease.
- The number of jobless claims remains high.
- The Federal Reserve has maintained the federal funds interest rate at a historically low level.
- Federal government intervention in the private sector has increased. Numerous financial institutions and automakers have received bailouts from the government.
- Millions of households owe more on their mortgages than their homes are currently worth. The number of residential home foreclosures continues to increase.
- The financial markets continue to experience instability—historic lows followed by rallies. In March 2009, the S&P 500 and Dow Jones Industrial Average reached their 12-year lows and NASDAQ closed at its lowest point since October 2002.
- The demand for U.S. Treasury bills has increased at a staggering rate, which drove the interest rate for these Treasury bills to less than 1 percent in March 2009.
- The Treasuries-Over-Euro-Dollar Spread reached 4.63 percent in October 2008, a historic high, before returning to 1.04 percent in March 2009.

Key Economic Indicators

.13 These key economic indicators further illustrate the severity of the recessionary period the United States is experiencing.

.14 The GDP measures output of goods and services by labor and property within the United States. It increases as the economy grows or decreases as it slows. According to advance estimates of the Bureau of Economic Analysis, real GDP decreased at an annual rate of 1.0 percent in the second quarter of 2009. This data indicates a moderation in the slowing of the economy seen in the fourth quarter of 2008 and first quarter of 2009, which experienced decreases of 6.3 percent and 5.5 percent, respectively.

.15 The unemployment rate began to level out in June, July, and August of 2009 when it was 9.5 percent, 9.4 percent, and 9.7 percent, respectively. An unemployment rate of 9.7 percent represents approximately 14.7 million people. Since the start of the recession in December 2007, the number of unemployed persons has increased by as much as 7.4 million or 4.8 percentage points. Despite the high level of unemployment across the U.S., in July 2009, jobs in the healthcare industry increased by 20,000. Of these new jobs, approximately 21 percent were in hospitals, 48 percent were in ambulatory care, and 29 percent were in nursing and residential care facilities.

.16 As of March 2009, the Federal Reserve had decreased the target for the federal funds rate more than 5.0 percentage points to less than 0.25 percent. The Federal Reserve noted in its August 12, 2009, press release "that economic conditions are likely to warrant exceptionally low levels of the federal funds rate for an extended period."

Government Intervention to Curtail the Economic Crisis

.17 The U.S. government has taken unprecedented actions to prevent worsening economic conditions, including passing the American Recovery and Reinvestment Act of 2009 (Recovery Act) and the Emergency Economic Stabilization Act of 2008 (EESA), facilitating the sale of ailing banks and dramatically increasing the monetary programs available from the Federal Reserve. The results of these actions have not been fully realized to date.

The American Recovery and Reinvestment Act of 2009

.18 In February 2009, President Obama signed legislation designed to work hand in hand with the EESA to stimulate the U.S. economy. The Recovery Act is designed primarily to combat the rising unemployment trends, put more money in the hands of consumers, and reduce the likelihood that state and local governments will need to raise taxes significantly. According to the White House press release, the legislation will do the following:

- Create or save 3.5 million jobs in the next 2 years
- Provide direct tax relief to working and middle class families
- Double the U.S. renewable energy generating capacity over 3 years
- Stimulate private investment in renewable energy through tax credits and loan guarantees
- Invest $150 billion in U.S. infrastructure projects
- Provide funds to U.S. state and local governments to support health and education programs

.19 Many of the provisions of this legislation took effect immediately in an effort to stimulate consumer spending and boost the economy. The total cost of the spending in the Recovery Act is $787 billion, which is in addition to the $700 billion in the EESA. Many economists are concerned that further financial support may be necessary before an economic recovery is possible. Additionally, the federal government developed the Web site www.recovery.gov to facilitate a transparent process to ensure accountability for the execution of the program.

.20 To monitor these funds on behalf of the federal government, a Recovery Act Accountability and Transparency Board has been created to review management of recovery dollars and provide early warning of problems. The seven member board includes Inspectors General and federal Deputy Cabinet secretaries. The Government Accountability Office (GAO) and the Inspectors General are provided additional funds and access for reviews of the act's funds and spending. The board is responsible for coordinating and conducting oversight of federal spending under the Recovery Act including, but not limited to, the following:

- Ensuring that funds are awarded and distributed in a prompt, fair, and reasonable manner.
- The recipients and uses of all funds are transparent to the public, and the public benefits of these funds are reported clearly, accurately, and in a timely manner.
- Funds are used for authorized purposes, and instances of fraud, waste, error, and abuse are mitigated.
- Projects funded under the Recovery Act avoid unnecessary delays and cost overruns.
- Program goals are achieved, including specific program outcomes and improved results on broader economic indicators.

.21 The Office of Management and Budget (OMB) will provide a supportive role to the board.

.22 OMB has published implementation guidance to the federal agencies on how they should carry out programs and activities enacted by the Recovery Act. The issuance of this guidance is happening on an as-needed basis; please check www.recovery.gov and www.whitehouse.gov/omb/recovery_default/ for current guidance. On April 3, 2009, OMB published implementation guidance for the Recovery Act. This is the second installment of detailed government-wide guidance for carrying out programs and activities enacted in the Recovery Act (Updated Implementing Guidance for the American Recovery and Reinvestment Act of 2009, M-09-15). This updated guidance supplements, amends, and clarifies the initial guidance issued by OMB on February 18, 2009 (Initial Implementing Guidance for the American Recovery and Reinvestment Act of 2009, M-09-10). Updates to the guidance are based on ongoing input received from the public, Congress, state and local government officials, grant and contract recipients, and federal personnel. The initial Recovery Act implementation guidance can be found at www.whitehouse.gov/omb/assets/memoranda_fy2009/m09-10.pdf, and the supplementary Recovery Act implementation guidance can be found at www.whitehouse.gov/omb/assets/memoranda_fy2009/m09-15.pdf. Questions and feedback about this memorandum or the guidance document can be addressed to recovery@omb.eop.gov and should have the term *guidance feedback* in the title of the e-mail. OMB will issue a subsequent memorandum clarifying any updates to the guidance based on feedback received.

Recovery Act Compliance Requirements

.23 For not-for-profit entities (NFPs), many new compliance requirements exist in the Recovery Act related to the receipt and use of funds. As required by Section 1512 of the Recovery Act, each recipient of federal funds under the Recovery Act must report the following information 10 days after each calendar quarter, beginning on October 10, 2009 (which will include the period from inception of the Recovery Act):

- The total amount of recovery funds received from each federal agency.
- The amount of recovery funds received that were obligated (encumbered) and expended to projects or activities. This reporting will also include unobligated federal allotment balances to facilitate reconciliations.
- A detailed list of all projects or activities for which recovery funds were obligated and expended, including the following:
  - — The name of the project or activity
  - — A description of the project or activity
  - — An evaluation of the project status of the project or activity
  - — An estimate of the number of jobs created and the number of jobs created and retained by the project or activity
- Detailed information on any subcontracts or subgrants awarded by the recipient, including the data elements required to comply with the Federal Funding Accountability and Transparency Act of 2006 (P.L. 109-282), allowing aggregate reporting on awards below $25,000 or to individuals.

.24 Readers should monitor the OMB Web site, www.whitehouse.gov/omb/, for further developments.

New Public Disclosure Requirements for Submissions to the Federal Audit Clearinghouse

.25 Included in the implementation guidance document M-09-10, discussed previously, is a requirement that all Single Audit reports received by the Federal Audit Clearinghouse (FAC) will be made available for public inspection on the internet. This requirement is effective for reports with fiscal years ending after September 30, 2009, and applies to all Single Audits, including those that have not received funding under the Recovery Act.

.26 A current concern with the FAC making the reports publicly available online is that a report may inadvertently include personally identifiable information (PII). Although the reports are currently subject to the Freedom of Information Act (FOI), the FAC sends all FOI requests to the Federal Cognizant agency, which is responsible for reviewing, redacting as necessary, and sending the reports to the requestor. Currently the FAC has an online system for federal agencies to access Single Audit reports. No current plan exists regarding how the FAC would respond to a FOI request for the whole database of reports and ensure PII is not disclosed. The OMB can direct the FAC to take proactive steps to ensure Single Audit reports do not include PII. Until such a system is in place, OMB recommends that entities and their auditors carefully review reports prepared for submission to the FAC to remove PII prior to submission.

AICPA Recovery Act Resource Center

.27 The AICPA Governmental Audit Quality Center (GAQC) helps member CPA firms meet the challenges of performing quality audits. The passage of the Recovery Act is certain to result in new challenges for auditors that perform audits under OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. This GAQC Resource Center is intended to allow auditors to more easily locate various GAQC Recovery Act communications, other related GAQC tools and resources, and links to other Web sites that may provide information to assist auditors going forward. The Recovery Act Resource Center is located at http://gaqc.aicpa.org/Resources/Recovery+Act+Resource+Center.htm.

Other Government Intervention

.28 The passage of the Recovery Act came shortly after the passage of the EESA, which was signed into law in October 2008. As stated in Section 2 of the EESA bill, it "provide[s] authority and facilities that the Secretary of the Treasury can use to restore liquidity and stability to the financial system of the United States" to ensure the economic well-being of Americans. Primary components of the EESA bill include the following:

- An allocation of $700 billion to stabilize the U.S. financial system
- The creation of an oversight board, executive compensation rules, and other corporate governance rules for any entities that receive government aid
- An increase of the statutory limit on public debt from $10.0 trillion to $11.3 trillion
- A temporary increase of Federal Deposit Insurance Corporation insurance limits
- The creation of a tax modification for Fannie Mae and Freddie Mac stock losses
- The restatement of the SEC's authority to suspend the application of FASB Statement No. 157, *Fair Value Measurements*, which is codified at FASB ASC 820, *Fair Value Measurements and Disclosures*
- The requirement of the SEC to conduct a study on the impact of FASB's fair value guidance[1]

.29 The EESA authorized the U.S. Treasury to create the Troubled Assets Relief Program (TARP), the original intent of which was to use $700 billion to purchase illiquid mortgage assets from banks. As part of TARP, the Capital Purchase Program (CPP) was intended to inject $250 billion of capital into banks. Half of the CPP funds were distributed to 9 of the largest financial institutions in the nation, which held approximately 55 percent of U.S. banking assets. The other half of the funds were allocated for smaller financial institutions. The

[1] For the full text of the Securities and Exchange Commission report, visit www.sec.gov/news/studies/2008/marktomarket123008.pdf.

clear intent of the CPP was for the participating banks to increase lending; however, many question if the banks have responded accordingly.

.30 In addition to bailout funds targeting financial institutions, a $17.4 billion rescue package for the U.S. automakers was issued in December 2008. The first $13.4 billion was lent to the automakers immediately, and the remaining $4 billion was lent in subsequent months. The U.S. government will continue to work directly with automakers and also will receive nonvoting warrants from automakers that accept taxpayer funding.

.31 The complete effects of the Recovery Act, as well as the other government interventions, will take time to be felt throughout the economy; however, the primary goal is to increase market confidence and liquidity.

Industry Trends and Conditions

The State of Health Care Entities

.32 In April 2009, the American Hospital Association (AHA) released the results of a survey of 1078 community hospital CEOs regarding the effect of the economic crisis on health care entities. The survey shows the following:

- The number of patients without insurance or other means to pay for health care is increasing, as is the number of patients covered by Medicaid or other low income assistance programs.
- A majority of hospitals have made cutbacks including staff reductions, administrative expense cuts, and elimination of available services.
- A 65 percent increase in the number of hospitals expecting to report a loss in the first quarter of 2009 when compared to a year earlier.
- Since 2008, 80 percent of respondents indicated that capital projects for facilities, clinical technology, or information systems have been postponed or eliminated, including some projects that were already in progress.
- There has been a substantial increase in the number of physician requests for hospitals to provide on-call pay or employment.

.33 More information about the AHA and the full survey results are available at www.aha.org.

Municipal Securities and Challenges in the Municipal Market

.34 In 2008, nearly $453 billion of municipal bonds and notes were sold to support a variety of public purposes. Additionally, over 10 million municipal trades occurred representing over $5.5 trillion in transactions during 2008. With approximately $2.7 trillion in principal value of securities outstanding and over 50,000 issuers, the municipal market continues to play a vital role in the U.S. economy.

.35 Beginning in late 2007 and throughout 2008, the municipal market experienced several dislocations related to the subprime mortgage crisis and associated turmoil in the credit markets. These included the downgrading of municipal bond insurers and the collapse of the municipal auction rate securities market.

.36 For many years, the credit enhancement provided by AAA-rated bond insurers was a prominent feature of the municipal securities market. As of the beginning of 2008, approximately 50 percent of all long-term municipal bonds were insured. However, credit rating agencies extensively downgraded bond insurers during 2008, primarily as a result of their exposure to subprime mortgage products. Hundreds of thousands of outstanding insured municipal bonds were affected by these downgrades. Use of bond insurance on new issues—something that, in previous years, had been used to help sell about half of all new issues—was used on only 18 percent of new issues during 2008.

.37 Another exceptional event during 2008 was the collapse in the $200 billion market for municipal auction rate securities (ARS). Prior to 2008, municipal auctions for these securities rarely failed. As the subprime mortgage crisis took hold and concerns over the credit quality of the bond insurance used on most ARS increased, auctions began to fail early in the year. Investor confidence in the auction process waned, which in turn, led to more auction failures and the collapse of the ARS market. All but about $78 billion in municipal ARS now has been restructured.

.38 General conditions in the municipal securities market have improved since the most extreme dislocations and liquidity shortages that occurred in the last quarter of 2008. Attracted by the higher yields, retail demand (particularly for high-grade credits) has been strong and has compensated for the loss of demand by many traditional institutional and leveraged accounts. Notwithstanding this general improvement, imbalances in supply and demand and illiquidity problems remain in certain segments of the market as of the early months of 2009. This is particularly true for lower rated issues and securities in certain market sectors such as housing.

The Credit Crisis and Its Potential Impact on Local Government Credit Ratings

.39 Local governments were put on notice in a recent report, *Impact of the Credit Crisis and Recession on Local Governments*, from the U.S. Public Finance division of Moody's Investors Service. The credit experts at Moody's believe that with the U.S. economic recession intensifying, and the continuing credit crisis limiting access to the credit markets, many local governments will face difficult fiscal choices, and some potentially may experience material stress over the next few years. The downturn in real estate values has heightened the general economy's impact on municipal governments' budgets, especially in local governments with a heavy reliance on property tax revenues. Moody's concludes that with the recession now appearing to have spread to most regions and sectors of the economy, few local governments will escape the difficult choice between raising taxes in the face of local economic stress and cutting services to balance their budgets. However, Moody's expects that the majority of municipalities will manage successfully through this period with a combination of spending cuts and revenue enhancement plans.

.40 The report concludes that although most municipalities have a reasonable degree of fiscal flexibility and demonstrated an ability to adapt to economic and fiscal cycles in the past, this recession is likely to be deeper and longer lasting than recent ones. As a result, Moody's said it expects that there will be a higher number of negative rating actions taken than in other recessions of the past 40 years, as some issuers experience disproportionate levels of stress that materially affect creditworthiness. The credit rating agency has said that its ratings actions will focus on municipal governments that experience higher levels of financial stress than comparably rated peers, and that additional downward rating pressure could result if this economic downturn proves exceedingly deep.

.41 Local governments with strong management teams, diverse revenue sources, predictable borrowing costs, and sound liquidity and reserves are expected to fare better than those without these characteristics and conditions. According to Moody's, generally speaking, the local government leadership's willingness to make necessary adjustments will be a key factor in maintaining that government's credit rating. For example, a municipality's failure to adjust its budget in a timely fashion could be considered a clear indicator of weak fiscal management and could place significant downward pressure on its credit rating.

.42 Auditors should consider whether a risk exists that the government's credit rating could be lowered and, if so, obtain an understanding of the effects that a reduced credit rating would have on the government's ability to fund its operations, or if a reduced rating would affect the government's outstanding debt obligations.

Legislative and Regulatory Developments

Uniform Prudent Management of Institutional Funds Act

.43 In July 2006, the National Conference of Commissioners on Uniform State Laws (NCCUSL) approved the Uniform Prudent Management of Institutional Funds Act (UPMIFA) and recommended it for enactment by the legislatures of the various states. UPMIFA is designed to replace the existing Uniform Management of Institutional Funds Act (UMIFA), which was approved by NCCUSL in 1972. The purpose of UMIFA was to provide uniform and fundamental rules for the investment of funds held by charitable institutions and the expenditure of donor-restricted funds as "endowments" to those institutions. The principles behind those rules were

- that assets would be invested prudently in diversified investments that sought growth as well as income, and
- that appreciation of assets could prudently be spent for the purposes of any endowment fund held by a charitable institution.

.44 Since its creation, UMIFA has been enacted in 47 states. In response to the increasing size and complexity of charitable endowments held in investments, UPMIFA was created based on the same principles. As of March 2009, UPMIFA has been enacted in 28 states and the District of Columbia and is pending legislation in 14 additional states. Although the basic principles are the same for UMIFA and UPMIFA, UPMIFA introduces the following new concepts:

- Historic-dollar-value is no longer recognized as the threshold below which an organization cannot spend from an endowment.
- Assets in an endowment fund are donor-restricted until appropriated.

- An optional provision (decided by each state) defining seven percent as a measure above which spending would be considered imprudent.

.45 In August 2008, FASB issued FASB Staff Position (FSP) FAS 117-1, *Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the* Uniform Prudent Management of Institutional Funds Act, *and Enhanced Disclosures for All Endowment Funds*, which is codified at FASB ASC 958-205, effective for fiscal years ending after December 15, 2008. The FSP

- provides guidance on the net asset classification of donor-restricted endowment funds for NFPs that are subject to an enacted version of UPMIFA.
- improves disclosures about an NFP's endowment funds (both donor-restricted and funds functioning as endowment), whether or not the NFP is subject to UPMIFA.

.46 The first, and perhaps most significant, question the FSP addresses is how UPMIFA's elimination of the historic-dollar-value threshold—the amount below which an NFP could not spend under UMIFA—affects net asset classification. The FSP requires an NFP to classify a portion of a donor-restricted endowment fund (other than a term endowment) as permanently restricted net assets. That portion would be equal to the amount of the fund (*a*) that must be retained permanently in accordance with explicit donor stipulations, or (*b*) that, in the absence of such stipulations, the NFP's governing board determines must be retained permanently, if any, under the relevant law. The NFP would be required to disclose its interpretation of the law. We anticipate that discussions among NFPs, accountants, attorneys, and regulators in the various individual states may lead to a consensus in those states determining what must be retained permanently under the law. If a governing board determines that the law requires maintenance of purchasing power of a donor's gift, the NFP would increase or decrease permanently restricted net assets to the extent that the purchasing power is maintained. (This would typically be done by adjusting permanently restricted net assets by an appropriate inflationary factor, such as the consumer price index [CPI] or higher education price index [HEPI].)

.47 In contrast, an NFP would not subsequently decrease permanently restricted net assets because of investment losses or organizational spending from the endowment but would, instead, decrease temporarily restricted net assets to the extent that donor-imposed temporary restrictions on net appreciation of the fund have not been met, or decrease unrestricted net assets. The guidance on investment losses and spending is consistent with the guidance previously provided on investment losses in FASB Statement No. 124, *Accounting for Certain Investments Held by Not-for-Profit Organizations*, paragraph 12 (codified at FASB ASC 958-205-45-22). FASB considered, but decided not to, change that guidance, noting that permanently restricted net assets should reflect the amount for which an NFP has a permanent fiduciary duty and not the amount that it has on hand at a financial statement date because of cumulative investment and spending decisions.

.48 The FSP also addresses whether two other provisions in UPMIFA's endowment spending guidelines impose temporary (time) restrictions on the portion of a donor-restricted endowment fund that would otherwise be considered unrestricted net assets:

- A provision that "[u]nless stated otherwise in the gift instrument, the assets in an endowment fund are donor-restricted assets until appropriated for expenditure by the institution"
- An optional provision for a rebuttable presumption that spending more than 7 percent of endowment market value is imprudent (Some states have included this provision, whereas others have not.)

.49 The FSP requires NFPs to apply the guidance previously provided in Emerging Issues Task Force (EITF) Topic No. D-49, "Classifying Net Appreciation on Investments of a Donor-Restricted Endowment Fund," included as an appendix to the FSP and which is also codified at FASB ASC 958-205. EITF Topic No. D-49 stresses that not all legal restrictions on the use of particular assets result in restricted net assets for accounting purposes, only those that extend donor restrictions. An example of the latter would be a requirement to maintain the purchasing power of a donor's endowment gift. Laws that refer to actions entirely within the purview of a governing board, such as acting to appropriate funds or exercising prudence do not, in and of themselves, extend donor imposed restrictions.

.50 The other key provisions of the FSP focus on improving disclosures both for donor-restricted and board-designated endowment funds. Aiming to improve transparency about endowments in an era of increased public scrutiny, the FSP focuses on disclosures in the following four areas:

- Net asset classification (especially how the classification is affected by a governing board's interpretation of relevant law)
- Spending policies
- Investment policies (especially their relationship with spending policies)
- Net asset composition and changes therein (especially the relationship of endowment spending to endowment size and growth)
- Reconciliation of beginning and ending balances of the endowment in total and by asset class

Centers for Medicare and Medicaid Services Activity

Medicare Payment Policy Changes

.51 The Centers for Medicare and Medicaid Services (CMS) is responsible for implementing payment systems to standardize amounts paid for healthcare services for Medicare patients. Each year, these fees schedules are reviewed against established criteria and adjusted accordingly. In July 2009, CMS announced proposed changes to policies and payment rates for services to be furnished during calendar year 2010.

.52 For inpatient services paid under the Hospital Inpatient Prospective Payment System (IPPS) and long-term care services paid under Long-Term Care Hospital Prospective Payment System (LCTH PPS), the final rule includes a 2.1 percent increase in rates and becomes effective beginning with discharges on or after October 1, 2009. The full text of the final rule can be found at http://frwebgate3.access.gpo.gov/cgi-bin/PDFgate.cgi?WAISdocID=1177376462+8+2+0&WAISaction=retrieve.

.53 For services provided by physicians and nonphysician practitioners who are paid under the Medicare Physician Fee Schedule (MPFS), proposed rates reflect a decrease of 21.5 percent. For outpatient services paid under the Hospital Outpatient Prospective Payment System (OPPS) and the Ambulatory Surgical Center Payment System (ASCPS), the proposed rule reflects an inflation increase of 2.1 percent. CMS accepted comments on the proposed rule until August 31 and will respond to all comments in a final rule to be issued by November 1, 2009. Unless otherwise specified, the new payment rates and policies will apply to services furnished to Medicare beneficiaries on or after January 1, 2010.

.54 For more information on the proposed rule, please visit www.federalregister.gov/inspection.aspx#special or www.archives.gov/federal-register/public-inspection/index.html.

.55 In addition, CMS is proposing two changes to address concerns from the Medicare Payment Advisory Commission (MedPAC) and the U.S. Government Accountability Office (GAO) about rapid growth in high cost imaging services. First, CMS is proposing to reduce payment for services that require the use of expensive equipment, which would produce a redistribution of the resulting savings to increase payments for other services, including primary care services. The current payment rates assume that a physician who owns this type of equipment will use it about 50 percent of the time, but recent survey data suggest that this expensive equipment is being used more frequently. As the use of this type of equipment increases, the per-treatment costs for purchasing, maintaining, and operating the expensive equipment declines, making a reduction in payment appropriate.

.56 Second, CMS is proposing to implement a requirement in the Medicare Improvements for Patients and Providers Act of 2008 that suppliers of the technical component of advanced imaging services be accredited beginning January 1, 2012, by designating accrediting organizations (AOs) for these suppliers and utilizing the imaging quality standards that have been developed by the AOs. The accreditation requirement would apply to mobile units, physicians' offices, and independent diagnostic testing facilities that create the images, but would not apply to the physician who interprets them. According to the GAO, spending on advanced imaging services, such as computed tomography (CT), magnetic resonance imaging (MRI), and positron emission tomography (PET), is growing almost twice as fast as spending on other types of imaging services and is a significant contributor to the rapid growth in health care spending in recent years, but little administrative oversight exists to ensure the quality of care. In a separate regulatory action, CMS will address suppliers' accountability, business integrity, physician and technician training, service quality, and performance management.

Medicare Recovery Audit Contractors

.57 The Medicare Modernization Act of 2003 authorized the Recovery Audit Contractors (RAC) demonstration project, initially a three-year demonstration project from March 2005 through March 2008 in California, Florida, and New York. It was expanded in 2007 to include Arizona, Massachusetts, and South Carolina. The Tax Relief and Healthcare Act of 2006, Section 302, mandated CMS to implement a permanent, nationwide RAC program no later than 2010.

.58 The RACs detect improper Medicare payments, correct the improper payments, and implement actions that will prevent future improper payments. The improper payments are to include both overpayments and underpayments to providers. According to CMS, the RAC demonstration project has identified $357.2 million in overpayments and $14.3 million in underpayments. The RACs are paid a contingency fee based on the amount of improper payments identified. This payment methodology has led to criticism that such an incentive could tempt RACs to identify errors where none exist.

.59 Four years of claims (from October 1, 2001 through September 30, 2005), were available for review under the RAC demonstration project. Under the permanent RAC program, the contractors will review claims paid on or after October 1, 2007, and at no time will they look back more than three years.

.60 The RACs have performed two types of reviews: automated reviews and complex medical reviews. The automated reviews were designed to identify the "low hanging fruit" and used data mining techniques to identify multiple units billed, missing modifiers, and payments for discontinued HCPC/CPT codes. The complex medical reviews involved reviewing the medical record or other documentation. They have led to a denial of payments mainly due to lack of medical necessity and missing records or documentation. The RACs were criticized in this area for failing to have knowledgeable and adequately trained staff performing the reviews and the lack of a medical director to interpret the medical records. RACs are now required to have a medical director.

.61 The RAC claim review process for medical records reviews includes the request by the RAC for the medical record or other documentation. Providers have 45 days to comply with the request. If the requested documentation is not submitted within the 45 days, the RAC may identify the claim as an overpayment by default. The RAC has 60 days to review the chart and issue a denial or an "all clear" letter to the provider.

.62 To dispute an RAC adjustment, providers can submit a rebuttal to the RAC or file an appeal following normal Medicare appeal rules. The provider must submit a rebuttal to the RAC within 15 days of the denial. The appeals process has various levels and strict deadlines that cannot be missed.

.63 An appeal must be filed soon after the RAC's notice of its decision (initial determination). The initial determination date is presumed to be five days after the date of the denial notice or the date of the take-back. The first level of appeal is to file an appeal or redetermination with the Medicare fiscal intermediary (FI) within 120 days after the initial determination. The second level of appeal is with a qualified independent contractor (QIC).

.64 After receiving the decision of the FI, the provider has 180 days to file an appeal with the QIC. The third level of appeal is with an administrative law judge (ALJ). This appeal must be filed within 60 days of the QIC decision. After the ALJ appeal, the next level of appeal is with the Medicare Appeals Council (MAC). This appeal must be filed within 60 days of the ALJ's decision. If the provider is still dissatisfied with the determination, the provider can file legal proceedings in U.S. District Court within 60 days of the MAC determination.

.65 Providers can prepare for the RAC program by developing a strategy and creating policies and procedures for addressing all RAC notifications. The strategy should address interdepartmental communication to notify clinical, reimbursement, and financial staff of any and all RAC requests. Providers should keep detailed records of all RAC requests, correspondence with the RAC, and the results of the determination.

.66 In the event of any denials, the provider should consider the value of filing a rebuttal or appeal by evaluating the financial impact, the cost versus the benefit of the appeal, and other factors such as availability and accuracy of the medical records and implications of not filing an appeal. Not filing an appeal could force the provider to institute changes in policies and procedures to address the issues raised in the RAC denials and could potentially expose the provider to higher scrutiny and increased medical audits.

.67 AICPA Auditing and Attestation Statement of Position (SOP) 00-1, *Auditing Health Care Third-Party Revenues and Related Receivables* (AICPA, *Technical Practice Aids*, AUD sec. 14,360), provides guidance about issues and risks related to revenue recognition and adjustments to revenues in subsequent periods that result from future program audits, administrative reviews, billing reviews, regulatory investigations, or other actions that are not resolved until future periods. The SOP also identifies certain responsibilities of management and of auditors related to revenue recognition and the related valuation estimates for receivables.

Status of the RAC Program

.68 By 2010, CMS plans to have four RACs in place. Each RAC will be responsible for identifying overpayment and underpayments in approximately one quarter of the country. The new RAC jurisdictions match the Durable Medical Equipment MAC jurisdictions. The RAC demonstration program has been deemed to be successful in returning dollars to the Medicare Trust Funds and identifying monies that need to be returned to providers. It has provided CMS with a new mechanism for detecting improper payments made in the past and has also given CMS a new tool for preventing future improper payments.

.69 On October 6, 2008, CMS announced the names of the new national RACs. The new RACs are as follows:

- Diversified Collection Services, Inc. of Livermore, California, in Region A, initially working in Maine, New Hampshire, Vermont, Massachusetts, Rhode Island, and New York.
- CGI Technologies and Solutions, Inc. of Fairfax, Virginia, in Region B, initially working in Michigan, Indiana, and Minnesota.
- Connolly Consulting Associates, Inc. of Wilton, Connecticut, in Region C, initially working in South Carolina, Florida, Colorado, and New Mexico.
- HealthDataInsights, Inc. of Las Vegas, Nevada, in Region D, initially working in Montana, Wyoming, North Dakota, South Dakota, Utah, and Arizona.

.70 Additional states will be added to each RAC region in 2009. More information on the status of the RAC program can be found at www.cms.hhs.gov.

Medicare Risk Adjusters

.71 Medicare Advantage Plans (plans) generally receive premium adjustments from CMS related to medical encounters that result in calculated risk score adjustments. These premium adjustments can be material to the financial statements of a plan. In addition to obtaining an understanding of a plan's process to estimate such premium adjustments, auditors should give appropriate consideration to whether the revenue recorded met the appropriate revenue recognition criteria and whether related receivables are collectible.

.72 Because of the complexities associated with estimating such premium adjustments, auditors may consult a specialist to assist in the design, and possibly performance of, related audit procedures. Further, auditors should assess the adequacy and appropriateness of a plan's related financial statement disclosures.

Municipal Securities Rulemaking Board Activity

.73 The Municipal Securities Rulemaking Board (MSRB), which develops rules for brokers, dealers, and banks engaged in underwriting, trading, and selling municipal securities, protects investors and ensures the integrity of the municipal market. The MSRB also operates information systems designed to promote transaction price transparency and access to municipal securities issuer disclosure documents.

Electronic Municipal Market Access

.74 One of the MSRB's top initiatives over the last year has been the development of its Electronic Municipal Market Access (EMMA) Web site, which provides improved disclosure and price transparency in the municipal market. Official statements and advance refunding documents for municipal bonds, real-time and historical trade data, interest rates and auction results for municipal auction rate securities, interest rates for variable rate demand obligations, daily market statistics, and educational material about municipal bonds are all available for free on EMMA (www.emma.msrb.org). The EMMA Web site is designed for use by individual investors but is also available to auditors, institutional investors, and municipal issuers so that any user easily can obtain free municipal securities disclosure documents from a single source.

.75 The data on the EMMA Web site comes from a number of sources. The MSRB collects primary market information and trade data for EMMA from underwriters and their agents. On July 1, 2009, the MSRB began collecting continuing disclosure documents from municipal issuers around the country and posting them for public availability within 15 minutes of receipt. The addition of these documents, and their availability to the public through EMMA, creates a complete repository of municipal bond disclosure documentation in a single location that is free and accessible 24-hours a day.

Continuing Disclosure

.76 Another phase of EMMA's development incorporates continuing disclosure documents provided by issuers into the integrated document display on EMMA. In December 2008 the SEC approved a proposal from the MSRB, which amends SEC Rule 15c2-12 (Title 17 CFR 240.15c2-12) to allow the expansion of EMMA to include these documents and to make the MSRB the central and only filing venue for these documents, replacing existing document depositories (that is, Nationally Recognized Municipal Securities Information Repositories and State Information Depositories). The change, effective July 1, 2009, has broad industry support because EMMA will provide a far more efficient and cost-effective system of document collection and dissemination. The MSRB is currently creating the necessary framework for issuers and their agents to submit continuing disclosure documents to EMMA in an all-electronic format and working to educate them about the process. Further information is available at www.msrb.org.

Other EMMA Features

.77 EMMA contains an extensive education center that provides in-depth information to help investors learn about the municipal bond market and better understand disclosure and trade price information provided through EMMA. Investors of all types, from beginners to those with advanced knowledge, can find useful information in the education center and through EMMA's Frequently Asked Questions (FAQ) section. The education center also includes the MSRB's industry-standard glossary of municipal securities terms.

Short-Term Obligation Rate Transparency System

.78 In 2009, the MSRB implemented its Short-term Obligation Rate Transparency (SHORT) system to increase transparency of municipal ARS and variable rate demand obligations (VRDOs). The SHORT system is the first centralized system for collection and dissemination of critical market information about ARS and VRDO. Information collected by the SHORT system is made available to the public, free of charge, on the MSRB's EMMA Web site.

.79 The SHORT system will be implemented in phases. The first phase collects and disseminates interest rate and descriptive information about ARS and VRDO. On January 30, 2009, the SHORT system became operational for ARS and, on April 1, 2009, for VRDO. This "interest rate information" allows market participants to compare ARS and VRDO across issues and track current interest rates. Included in this information is the current interest rate, the length of the interest rate reset period, as well as characteristics of the security, such as the identities of broker-dealers associated with the operation of the securities. This system is a useful tool for both auditors and their clients to evaluate, assess, and value relevant securities.

.80 Later phases of this initiative to increase transparency of ARS and VRDO include the collection and dissemination of ARS bidding information. This information will allow market participants to obtain important information about the liquidity of an ARS and greater granularity into the results of the auction process. In addition, the MSRB plans to collect ARS documents that describe auction procedures and interest rate setting mechanisms as well as VRDO documents that describe the provisions of liquidity facilities, such as letters of credit and standby bond purchase agreements. More information about the SHORT system is available at www.msrb.org/msrb1/whatsnew/2008-49.asp.

Bank Tying

.81 On August 14, 2008, the MSRB issued Notice 2008-34, *Notice on Bank Tying Arrangements, Underpricing of Credit and Rule G-17 on Fair Dealing*. In 2008, there was a major increase in demand for bank letters of credit and bank liquidity facilities by state and local government issuers of VRDOs. Some issuers of outstanding VRDOs were seeking to substitute letters of credit for bond insurance provided by downgraded monoline insurers. Other issuers were seeking to issue VRDOs to refund auction rate securities after auctions began to fail. The MSRB was concerned that, as a result of this increase in demand for letters of credit and liquidity facilities (bank facilities), some banks might consider proposing to issuers that they would receive a bank facility if their securities affiliates were selected as underwriters or remarketing agents for the issuer's VRDOs. There was also concern that banks might offer to price bank facilities on below market terms in return for underwriting or remarketing business for their securities affiliates. Notice 2008-34 reminded bank-affiliated dealers that federal prohibitions exist on such tying or underpricing arrangements, and that a dealer who aids or abets such arrangements would also violate MSRB Rule G-17, *Conduct of Municipal Securities Activities*. The full text of the notice is available at www.msrb.org/msrb1/archive/2008/2008-34.asp.

IRS Activity

Department of Treasury and IRS Issue Priority Guidance Plan for 2009

.82 Fiscal year 2009 priorities are addressed through a flexible and interdisciplinary array of new tools that focus on enforcement of the tax law and improving customer service. Priorities include the following:

- Implementing a voluntary compliance program for delinquent filers
- Addressing the issue of donor control and noncash contributions
- Continuing a variety of compliance projects that focus on areas such as charitable spending initiatives, gifts-in-kind, educational institutions, hospitals, and community foundations
- Initiatives focused on identifying nonfilers in the gaming, employment tax, and tax-exempt entity areas
- A further focus on transparency and governance by tax exempt entities
- Developing a new compliance guide, known as a *cyber assistant*, and formal guidance on hot topics such as Form 990 revisions

.83 Additional information on these and other topics is available at www.irs.gov/pub/irs-tege/finalannualrptworkplan11_25_08.pdf.

Form 990 Redesigned for Tax Year 2008

.84 In December 2007, the IRS issued an updated version of Form 990 for tax year 2008 (which will be filed in 2009) to enhance transparency, promote tax compliance, and minimize the burden on the filing organization. Form 990 now consists of an 11-page core form, which is to be completed by all filers, and 16 schedules designed by topic (lobbying, related parties, compensation, and so on). A transition period allows smaller organizations and certain schedules pertaining to hospitals and tax-exempt bonds to use Form 990-EZ.

.85 Substantial changes have been made to the amount and type of information required on the new Form 990. Some of the more significant changes include the following:

- More questions regarding organizational governance practices
- Disclosure of information from the organization's audited financial statements
- Expansion of compensation information disclosures
- Expansion of disclosures regarding programs and activities of the organization

New Form 990 Schedule for Hospitals

.86 Of special interest is the new Schedule H, "Hospitals," to be completed by organizations that operate one or more facilities licensed, registered, or similarly recognized as a hospital under state law. The purpose of this schedule is to obtain information regarding the community benefit activities of not-for-profit hospitals and to collect other information about the practices and policies of the hospital. Schedule H consists of the following six parts:

- *Part I, Charity Care and Certain Other Community Benefits at Cost.* Requires reporting of charity care policies, the availability of community benefit reports, and the cost of charity care and other community benefit programs such as charity care at cost, unreimbursed Medicaid, and other means-tested government programs; community health improvement services and community benefit operations; health professions education and training; subsidized health services; research; and cash and in kind contributions to community groups.
- *Part II, Community Building Activities.* Provides for reporting of the cost of various kinds of community building activities.
- *Part III, Bad Debt, Medicare, & Collection Practices.* Requires reporting of bad debt expense and Medicare shortfalls at cost and other information relating to such items.
- *Part IV, Management Companies and Joint Ventures.* Requires information regarding certain joint ventures and management companies in which the organization's officers, directors, trustees, key employees, and medical staff or employed physicians have an aggregate ownership percentage exceeding 10 percent of such entity in addition to any related organization or joint venture reporting required in Schedule R.
- *Part V, Facility Information.* The organization must separately list each facility that is licensed, registered, or similarly recognized by state law as a health care facility (hospital or otherwise).
- *Part VI, Supplemental Information.* Requires information pertinent to determining how the organization is serving its communities, including community needs assessments, education of patients about eligibility for charity care and government assistance programs, relationships with others in an affiliated system, and descriptions that supplement responses to the other parts of the schedule.

.87 Schedule H will be phased in beginning in 2008. For 2008 tax years, only Part V, Facility Information, will be required to be completed so that basic identifying information regarding the organization's facilities is collected. All other parts of Schedule H are optional for 2008. The entire Schedule H must be completed for tax years beginning in 2009. More information is available at www.irs.gov/charities/index.html.

New IRS Regulation on Required Withholding

.88 IRS Proposed Regulations REG-158747-06 were published in the Federal Register on December 5, 2008, for new IRC subsection 3402(t). This subsection, created by the Tax Increase Prevention and Reconciliation Act of 2005, originally required that payments by governmental entities for goods or services after December 31, 2010, are subject to 3 percent income tax withholding, with some exceptions. The implementation date has now been changed by the Recovery Act and applied to payments after December 31, 2011. Although this proposed regulation will not affect audits in 2009, auditors may want to bring the issue to the attention of their clients.

.89 These new withholding requirements would apply to payments greater than $10,000 made by

- the entire U.S. government, including all federal agencies, the executive branch, the legislative branch, and the judicial branch.
- all states, including the District of Columbia (but not including Indian tribal governments).
- all political subdivisions of a state government or every instrumentality of such subdivisions unless the instrumentality makes annual payments for property or services of less than $100 million.

.90 Generally, withholding would be required on all payments to all persons providing property or services to the government, including individuals, trusts, estates, partnerships, associations, and corporations. Withholding would occur at the time of payment and applies to payment in any form (cash, check, credit card, or payment card). If the government entity fails to withhold the tax required under Section 3402(t), it becomes liable for the payment of the tax.

.91 The proposed regulations provide the following exceptions from the withholding requirements:

- Payments otherwise subject to withholding, such as wages.
- Payments for retirement benefits, unemployment compensation, or social security.
- Payments subject to backup withholding, if the required backup withholding is actually performed.
- Payments for real property.
- Payment of interest.
- Payments to other government entities, foreign governments, tax exempt organizations, or Indian tribes.
- Payments made under confidential or classified contracts, as described in IRC 6050M(e)(3).
- Payments made by a political subdivision of a state or instrumentalities of a political subdivision of a state that make annual payments for property of services of less than $100 million.
- Public assistance payments made on the basis of need or income. However, assistance programs based solely on age, such as Medicare, are subject to the requirements.

P1: G.Shankar
ACPA108-01 ACPA108.cls September 29, 2009 15:31

- Payments to employees in connection with service, such as retirement plan contributions, fringe benefits, and expense reimbursements under an accountable plan.
- Payments received by nonresident aliens and foreign corporations.
- Payments made by Indian tribal governments.
- Payments in emergency or disaster situations.

.92 For more details, please see the Proposed Regulations, which can be accessed at www.regulations.gov/fdmspublic/component/main?main=DocumentDetail&o=09000064807ce036.

E-Postcard Required for Small Exempt Entities

.93 Beginning in 2008, exempt entities with gross receipts under $25,000 must make an annual electronic filing with the IRS using Form 990-N, *Electronic Notification (e-postcard) For Tax-Exempt Organizations Not Required to File Form 990 or 990–EZ*. The e-postcard is due in 2009 for tax years beginning on or after January 1, 2008. If an entity that is required to file fails to do so for three consecutive years, it will lose its tax exempt status. For more information and a link to the e-postcard, go to www.irs.gov/charities/article/0,,id=169250,00.html.

Internet-Based Workshop for Exempt Entities

.94 The IRS has a Web-based version of its popular Exempt Organizations Workshop covering tax compliance issues confronted by small- and mid-sized tax exempt entities.

.95 The free online workshop, *Stay Exempt—Tax Basics for 501(c)(3)s*, consists of five interactive modules on tax compliance topics for exempt entities:

- *Tax-Exempt Status*—How can you keep your 501(c)(3) exempt?
- *Unrelated Business Income*—Does your entity generate taxable income?
- *Employment Issues*—How should you treat your workers for tax purposes?
- *Form 990*—Would you like to file an error-free return?
- *Required Disclosures*—To whom are you required to show your records?

.96 Users can access this new training program at www.stayexempt.org. Users can complete the modules in any order and repeat them as many times as they like. The online training Web site does not require registration, and its visitors will remain anonymous.

Fast Track Settlement Program

.97 In December 2008, the IRS announced an opportunity for entities with issues under examination by the Tax Exempt and Governmental Entities Division (TE/GE) to use Fast Track Settlement (FTS) to expedite case resolution. The TE/GE FTS will enable TE/GE entities that currently have unresolved issues in at least one open period under examination to work together with TE/GE and the Office of Appeals (Appeals) to resolve outstanding disputed issues while the case is still in TE/GE jurisdiction. TE/GE and Appeals will jointly administer the TE/GE FTS process. TE/GE FTS will be used to resolve factual and legal issues, and it may be initiated at any time after an issue has been fully developed, but before the issuance of a 30-day letter or its equivalent. TE/GE FTS will be available to taxpayers for a pilot period of up to 2 years, beginning in December 2008. Upon completion of the 2-year pilot period, TE/GE and Appeals will evaluate the program, consider necessary adjustments, and determine whether to make the program permanent. More information is available at www.irs.gov/irb/2008-48_IRB/ar14.html#d0e2519.

Resource Materials—Compliance Initiatives for Tax-Exempt Entities

.98 The Exempt Organization Division of the IRS has made materials available that were used in or which discuss its compliance initiatives including colleges and universities, limited liability company projects, community foundations, bond compliance, hospitals, and executive compensation. You can find this material at www.irs.gov/charities/article/0,,id=162493,00.html.

Listing of Published Guidance—2009

.99 Readers should be aware that the IRS Web site contains a digest of published guidance for tax exempt entities issued in 2009 at www.irs.gov/charities/content/0,,id=202419,00.html. The published guidance includes treasury regulations, revenue rulings, revenue procedures and notices, and announcements of recently published issues of interest to tax-exempt entities.

.100 Additionally, the IRS Web site also contains an archive that presents digests of IRS-published guidance of interest to tax-exempt entities for the years 1954–2008. The archived guidance can be found at www.irs.gov/charities/article/0,,id=151053,00.html.

"Red Flags" Rule

.101 In October 2007, the Federal Trade Commission (FTC) issued the "Red Flags" rule for financial institutions and creditors to fight identity theft. The rule sets out how certain businesses and organizations must develop, implement, and administer their identity theft prevention programs. These programs must include the following four basic elements, which together, create a framework to address the threat of identity theft.

1. The program must include reasonable policies and procedures to identify the "red flags" of identity theft that may arise in the day-to-day operation of your business. Red flags are suspicious patterns or practices or specific activities that indicate the possibility of identity theft. For example, if a customer has to provide some form of identification to open an account with an entity, an ID that looks like it might be fictitious would be a "red flag."

2. The program must be designed to detect the red flags that have been identified. For example, if an entity has identified fake IDs as a red flag, it must have procedures in place to detect possible fake, forged, or altered identification.

3. The program must spell out appropriate actions to take when red flags are detected.

4. The program must address how the program will be reevaluated periodically to reflect new risks from this crime because identity theft is an ever-changing threat.

.102 The program must state who is responsible for implementing and administering it effectively. Because employees have a role to play in preventing and detecting identity theft, the program also must include appropriate staff training. The program also must address the manner in which contractors will be monitored when outsourcing or subcontracting functions of operations that would be covered by the rule.

.103 The Red Flags rule applies to financial institutions and creditors. The rule requires a periodic risk assessment to determine if the entity has covered accounts. A written program needs to be in place only if the entity has covered accounts. It is important to look closely at how the rule defines *financial institution* and *creditor* because the terms apply to groups that typically might not use those words to describe themselves. For example, many not-for-profit entities and government agencies are creditors under the rule.

.104 Health care entities need to implement the Red Flags rule if they defer payment for goods or services. An example would be payment plans for medical services. Because of their creditor status in these situations, the Red Flags rule applies.

.105 The FTC suspended enforcement of the new Red Flags rule until May 1, 2009, to give creditors and financial institutions additional time in which to develop and implement written identity theft prevention programs. This deferral by the FTC does not affect other federal agencies' enforcement of the original November 1, 2008, deadline for institutions subject to their oversight to be in compliance.

.106 More information and a document outlining specific requirements of the Red Flags rule can be found at http://ftc.gov/redflagsrule.

Audit and Attestation Issues and Developments

Audit Risks Arising From Current Economic Conditions

.107 The recent economic conditions and regulatory actions described in this alert may cause additional risk factors that had not previously existed or did not have a material effect on audit clients in prior years. Some risks that may affect an entity in the current economic environment are as follows:

- Constraints on the availability of capital and credit
- Going concern and liquidity issues
- Marginally achieving explicitly stated strategic objectives
- Use of off-balance-sheet financing
- Special-purpose entities, joint ventures, or other complex financing arrangements
- Volatile real estate and business markets
- The credit crisis, which can cause significant measurement uncertainty, including accounting estimates and fair value measurements

.108 Although many of these risks are not new to businesses, consideration of the ways a client is affected by external forces is part of obtaining an understanding of the entity and its environment and will allow the auditor to plan and perform the audit to address those risks. As noted in paragraph .17

of AU section 312, some possible audit responses to a significant risk of material misstatement include increasing the extent of audit procedures, performing procedures closer to year-end, or increasing audit procedures to obtain more persuasive evidence. Additionally, given the constant changing status of economic conditions that could affect your client, auditors should consider modifying audit procedures to ensure that risks are still adequately addressed.

.109 Although it is impossible to predict and include all accounting, auditing, and attestation issues that may affect your engagements, we cover the primary areas of concern given the current economic conditions in this alert. Continue to remain alert to economic, legislative, and regulatory developments, as well as the associated accounting, auditing, and attestation issues as you perform your engagements.

Liquidity Considerations

.110 Technical Questions and Answers (TIS) section 1100.15, "Liquidity Restrictions" (AICPA, *Technical Practice Aids*), addresses potential accounting and auditing implications when a fund or its trustee imposes restrictions on a nongovernmental entity's ability to withdraw its balance in a money market fund or other short-term investment vehicle. This question and answer section discusses some considerations for when these restriction events occur, such as determining (*a*) whether any assets subject to these restrictions qualify as cash equivalents or current assets; (*b*) whether disclosures about the risks and uncertainties resulting from such restrictions should be made; (*c*) whether these restrictions may trigger violations of debt covenants and, if so, if that liability should be classified as current; (*d*) whether the financial statements need to be adjusted if the occurrence of such restriction occurs between the balance sheet date and the issuance date; and (*e*) whether the restriction events call into question the entity's ability to continue as a going concern.

.111 Auditors should consider whether any additional disclosures made by management include forward-looking statements that are not required by generally accepted accounting principles (GAAP) and, therefore, may not be audited. Auditors also should consider whether the inability to withdraw funds can pose significant challenges to the entity's liquidity and, therefore, affect the entity's ability to continue as a going concern. Restrictions on liquidity also may be an appropriate matter to communicate to those charged with governance. Finally, the auditor should consider if he or she wishes to emphasize any liquidity restrictions in the auditor's report. For further details, see the question and answer at www.aicpa.org/download/acctstd/TIS1100_15.pdf.

Alternative Investments

.112 The AICPA practice aid *Alternative Investments—Audit Considerations* is a useful tool for auditors that focuses on the existence and valuation assertions associated with alternative investments but also discusses general considerations pertaining to auditing alternative investments, management representations, disclosure of certain significant risks and uncertainties, and reporting. As defined in the foreword of the practice aid, alternative investments are

> investments for which a readily determinable fair value does not exist . . . includ[ing] private investment funds meeting the definition of an investment company . . . such as hedge funds, private equity funds, real estate funds, venture capital funds, commodity funds, offshore

fund vehicles, and funds of funds, as well as bank common/collective trust funds.

.113 You can access the full text of this practice aid on the AICPA's Web site at www.aicpa.org/Professional+Resources/Accounting+and+Auditing/Audit+and+Attest+Standards/Practice+Aids+and+Tools/alternative_investments.htm.

.114 Given the state of the economy, many funds are imposing limitations on redemptions, and some are even unwinding. As this occurs, the fair value measurements applied to these investments will fall under increased scrutiny and become even more important.

Auditing Fair Value Measurements

.115 In addition to understanding the looming questions relative to fair value accounting, auditors should be aware of audit issues involving fair value accounting. Particular assets, liabilities, and components of equity are measured or disclosed at fair value in the financial statements, and it is management's responsibility to make the fair value measurements and disclosures. When auditing these fair values to ensure they are in conformity with GAAP, auditors should consult AU section 328, *Auditing Fair Value Measurements and Disclosures* (AICPA, *Professional Standards*, vol. 1), which establishes standards and provides guidance for auditors. Specific types of fair value measurements are not covered by AU section 328. For example, when auditing the fair value of derivatives and securities, refer to AU section 332, *Auditing Derivative Instruments, Hedging Activities, and Investments in Securities* (AICPA, *Professional Standards*, vol. 1).

.116 In regard to analyzing the sufficiency of the audit evidence, the strongest audit evidence to support a fair value is an observable market price in an active market. If that is not available, a valuation method should incorporate common market assumptions. If common market assumptions are not available or require significant adjustments, the entity may use its own assumptions. The auditor should obtain an understanding of the entity's process for determining fair values, as well as whether the fair value measurements and disclosures are in accordance with GAAP. During this testing, the auditor also may identify any possible indicators of impairment. According to paragraph .23 of AU section 328, substantive tests of the fair value measurements may involve (*a*) testing management's significant assumptions, the valuation model, and the underlying data; (*b*) developing independent fair value estimates for corroborative purposes; or (*c*) reviewing subsequent events and transactions. Paragraph .26 also notes that when testing the fair value measurements and disclosures, the auditor evaluates whether management's assumptions are reasonable and reflect, or are not inconsistent with, market information. In relation to FASB ASC 820, this might include whether the market is distressed, whether the transaction was an orderly transaction, the reasonableness of the determination within the fair value hierarchy of inputs, and the reasonableness of the underlying assumptions.

Fair Values of Securities

.117 The guidance in AU section 332 relating to auditing the fair value of securities is fairly similar to the guidance in AU section 328; however, there are some items of note for the auditor. As previously mentioned, quoted market prices in active markets are the best available audit evidence to support a fair value; however, when they are unavailable and the valuations of securities are obtained from a broker or dealer or another pricing service based on valuation models, the auditor should understand the underlying valuation method used (such as a cash flow projection). These prices also may be based on quoted prices from an active market or other observable inputs that will be a consideration on the auditor's procedures, as well. The process used by the pricing service in measuring fair value should be evaluated to determine the consistency with the specified valuation method (typically fair value, as defined in FASB ASC 820-10-20). The auditor also may determine that it is necessary to obtain quotes from more than one pricing source based on circumstances, such as an existing relationship between the entity and the valuing entity, which could inhibit objective pricing or underlying valuation assumptions that are highly subjective. In the context of FASB ASC 820, quoted prices in active markets are considered level 1 inputs.

.118 When an entity performs its own valuation, value testing procedures include the following:

- Assessing the reasonableness
- Comparing the assumptions to industry reports or benchmarks
- Assessing the appropriateness of the model
- Calculating the value using his or her own model
- Comparing the fair value with subsequent or recent transactions

.119 Whether the inputs to the entity's valuation model are observable determines their characterization as level 2 or level 3 inputs, respectively, within FASB ASC 820. When extensive judgment is needed, consider using a specialist or refer to AU section 342, *Auditing Accounting Estimates* (AICPA, *Professional Standards*, vol. 1). Additionally, when the underlying collateral of a security significantly contributes to its fair value and collectibility of the security, evidence of the collateral also should be examined for existence, fair value, transferability, and the investor's right to the collateral.

.120 Paragraph .19 of AU section 328 also notes that the auditor should evaluate whether the entity's method for determining fair value measurements is applied consistently and, if so, whether the consistency is appropriate considering possible changes in the environment or circumstances affecting the entity or changes in accounting principles. The auditor also should evaluate management's conclusions regarding other-than-temporary impairment on its securities. Examples of factors that could cause an other-than-temporary impairment, per paragraph .47 of AU section 332, include the following:

- Fair value is significantly below cost and
  - — the decline is attributable to adverse conditions specifically related to the security or to specific conditions in an industry or in a geographic area.
  - — the decline has existed for an extended period of time.
  - — management does not possess both the intent and the ability to hold the security for a period of time sufficient to allow for any anticipated recovery in fair value.
- The security has been downgraded by a rating agency.
- The financial condition of the issuer has deteriorated.

- Dividends have been reduced or eliminated, or scheduled interest payments have not been made.
- The entity recorded losses from the security subsequent to the end of the reporting period.

.121 Auditors must consider all facts and circumstances when determining if an other-than-temporary impairment has occurred. Additionally, the classification of an entity's securities is based on management's intent and ability. The auditor should obtain an understanding of management's classification process among trading, available-for-sale, and held-to-maturity, as well as consider the classifications in light of the entity's current financial position.

Auditing Accounting Estimates

.122 As noted in paragraph .04 of AU section 342, the auditor is responsible for evaluating the reasonableness of accounting estimates made by management in the context of the financial statements as a whole. Although this alert has discussed fair value measurements at length, it is important to remember many types of accounting estimates exist in client financial statements. Some examples include the allowance for uncollectible accounts receivable, impairment analysis and estimated useful lives of long-lived assets, valuation allowance for deferred tax assets, and actuarial assumptions in pension and other postretirement benefit costs.

.123 Given the current economic climate, additional skepticism should be exercised when considering management's underlying assumptions used in accounting estimates. When evaluating accounting estimates, the auditor should consider both the subjective and objective factors with professional skepticism. As discussed in paragraph .09 of AU section 342, key factors and assumptions that the auditor normally concentrates on include the assumptions that are significant to the estimate, sensitive to variations, deviations from historical patterns, or particularly subjective and susceptible to misstatement and bias; however, it is important to consider whether historical patterns are still applicable.

.124 For example, in the current slow market, new patterns may emerge. In this economic climate, with possible increasing pressure on management to meet earnings, a key aspect of AU section 342 is for an auditor to determine the reasonableness of management's accounting estimates with an extra degree of professional skepticism. As noted by AU section 316, *Consideration of Fraud in a Financial Statement Audit* (AICPA, *Professional Standards*, vol. 1), when assessing audit differences between client estimates and audit estimates, even if they are individually reasonable, an auditor should consider whether these differences are indicative of possible bias by management. If so, the auditor should reconsider the estimates as a whole.

.125 The auditor should obtain an understanding of how management develops estimates and should employ one of the approaches outlined in paragraph .10 of AU section 342 in testing that process. In reviewing and testing management's process, the auditor may consider identifying controls around this process and determining if the underlying data used for the estimate are reliable and used appropriately. An auditor also may develop an estimate and compare it to management's estimate. Lastly, the auditor may review subsequent events or transactions occurring prior to the date of the auditor's report. Further, as noted in AU section 316, hindsight may provide the auditor additional insight into the existence of management bias. For further details on auditing estimates, see AU section 342.

Using the Work of a Specialist

.126 It may be necessary to use a specialist (such as a securities valuation expert) to assist in auditing complex or subjective matters. Examples of matters in which an auditor may engage a specialist are valuation issues; reasonableness of determination of amounts derived from specialized techniques or models; or implementation of technical requirements, regulations, or legal documents. AU section 336, *Using the Work of a Specialist* (AICPA, *Professional Standards*, vol. 1), provides guidance to auditors in using specialists. The guidance in AU section 336 is applicable when the specialist is hired by management or if the auditor engages the specialist. However, if a specialist employed by the auditor's firm participates in the audit, AU section 311, *Planning and Supervision* (AICPA, *Professional Standards*, vol. 1), is applicable rather than AU section 336.

.127 When using the work of a specialist, the auditor should evaluate the specialist's professional qualifications, obtain an understanding of the nature of the work performed or to be performed, and evaluate the relationship of the specialist to the client in terms of objectivity. Although the appropriateness and reasonableness of the methods and assumptions employed by the specialist are his or her responsibility, the auditor should obtain an understanding of these qualities, test the underlying data provided to the specialist, and evaluate the specialist's findings in the context of the audit and related assertions in the financial statements.

Consideration of an Entity's Ability to Continue as a Going Concern

.128 The consideration of an entity's ability to continue as a going concern is required in every audit performed under generally accepted auditing standards and is an especially important consideration in the current state of the economy. An entity's ability to continue as a going concern is affected by many factors related to the current uncertain economy, such as the industry and geographic area in which it operates, the financial health of its customers and suppliers, and financing sources.

.129 As explained by paragraph .02 of AU section 341, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern* (AICPA, *Professional Standards*, vol. 1), the auditor's evaluation is based on his or her knowledge of relevant conditions and events that exist at or have occurred prior to the date of the auditor's report. Therefore, this is an ongoing evaluation that extends through the date of the auditor's report.

.130 The auditor has a responsibility to evaluate whether a substantial doubt exists about the entity's ability to continue as a going concern for a reasonable period of time. AU section 341 notes that is a period not to exceed one year beyond the date of the financial statements being audited.

.131 Audit teams may find it useful to have preliminary discussions about going concern considerations during engagement planning meetings; however, as noted in AU section 341, it is not necessary to design audit procedures around specifically identifying the possibility of a going concern because results of typical audit procedures should illuminate any indicators. These procedures may consist of analytical procedures, review of subsequent events, review of compliance with financing agreements, review of board minutes, inquiry of legal counsel, and confirmation with related third parties of the details of arrangements to provide or maintain financial support.

.132 Some risks related to the current state of the economy that may influence an entity's ability to continue as a going concern include the following:

- Lenders may be looking for ways to withdraw from lending relationships.
- Financial support of a related party may not be a feasible mitigating factor, depending on the financial health of that related party.
- An entity's financial health could be significantly weakened if their suppliers or customers have been strongly affected by the economic crisis.
- Projections provided by entities based on historical data may not be reliable future predictions.
- Some entities may be hesitant to include informative and transparent going concern disclosures.

.133 If the auditor believes a substantial doubt on the entity's ability to continue as a going concern exists, the next steps are to obtain management's plans to mitigate the effect of such conditions and then assess the likelihood that these plans can be effectively implemented. Additionally, auditors may consider posing the following questions to help make their assessment on the likelihood of management's plans to successfully mitigate their going concern risk:

- What is the strategy for extending lines of credit or refinancing any debt coming due? Have any preliminary agreements or discussions occurred?
- If negative operating trends exist, how does management plan on turning them around?
- If turnover of key personnel has occurred, what actions are being taken to replace these positions?
- What is the plan to maintain or increase the liquidity of your balance sheet?
- Do any restrictions exist that could limit management's ability to carry out these plans?

.134 If, after considering management's plan, an auditor determines a substantial doubt about an entity's ability to continue as a going concern for a reasonable period of time remains, the auditor should communicate with those charged with governance of the entity, in accordance with AU section 341. In that instance, the auditor also should consider the effects on the entity's financial statements and the adequacy of the related disclosure, and an explanatory paragraph should be added to the audit report following the opinion paragraph.

.135 Alternatively, if management's plan mitigates the risk of the entity's ability to continue as a going concern, the auditor should consider disclosing the primary conditions that gave rise to the initial doubt and management's plans. These disclosures are especially important for financial statement users to fully comprehend the entity's financial strength and ability to continue as a going concern.

.136 FASB has undertaken a project that will relocate the guidance related to going concern from the realm of auditing standards to accounting standards. See the "On the Horizon" section of this alert for further details.

Consideration of Fraud in a Financial Statement Audit

.137 AU section 316 is the primary source of authoritative guidance about an auditor's responsibilities concerning the consideration of fraud in a financial statement audit. AU section 316 establishes standards and provides guidance to auditors in fulfilling their responsibility to plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement, whether caused by error or fraud, as stated in paragraph .02 of AU section 110, *Responsibilities and Functions of the Independent Auditor* (AICPA, *Professional Standards*, vol. 1).

.138 Three conditions generally are present when fraud occurs:

- Management or other employees have an incentive or are under pressure, which provides a reason to commit fraud.
- Circumstances exist (for example, the absence of controls, ineffective controls, or the ability of management to override controls) that provide an opportunity for a fraud to be perpetrated.
- Those involved are able to rationalize committing a fraudulent act.

.139 The current economic situation may result in unexpected losses and possibly cause financing or liquidity difficulties for many entities. Additionally, management may be valuing many illiquid securities using inherently subjective methodologies. These situations may provide management additional opportunity and incentive to commit fraud.

.140 As seen in the news recently, a number of frauds that include the three previously mentioned conditions allegedly have occurred. One of those frauds is that of Bernard Madoff Investment Securities. Auditors should ensure they are properly testing for the existence of assets, such as investments, in this scenario. Additionally, auditors should always gain an understanding of the entity's business and how profits are made. In the Madoff case, auditors are being probed about failing to question the strong, consistent annual returns by these investment funds that lacked a clear investment strategy. Because of the characteristics of fraud, the auditor's exercise of professional skepticism is important when considering the risks of material misstatement due to fraud.

.141 Professional skepticism is an attitude that includes a questioning mind and a critical assessment of audit evidence. The auditor should conduct the engagement with a mindset that recognizes the possibility that a material misstatement due to fraud could be present, regardless of any past experience with the entity and regardless of the auditor's belief about management's honesty and integrity. Furthermore, professional skepticism requires an ongoing questioning of whether the information and evidence obtained suggests that a material misstatement due to fraud has occurred. AU section 316 provides additional information, including ways for the auditor to respond to the risk of material misstatement due to fraud.

Evaluating the Existence of Assets

.142 The Madoff case, and other recent fraud investigations, brings to light a number of risks that continually need to be considered and responded to by management and auditors. Due to the nature of securities and other financial instruments, determining and testing the ownership and existence of investments has become more difficult. Often, securities and other investments purchased on behalf of an entity are held in the name of a broker organization, which may or may not be a custodian; generally, custodians do not obtain a paper document, only an electronic record of the assets.

.143 Some examples of risks inherent in investment transactions that may be relevant when assessing the existence of investments are as follows:

- The assets involved may not be readily available to physical inspection.
- There could be a lack of effective, independent, third party oversight.
- The information received from a broker organization in the form of monthly statements or in response to audit confirmation requests, may require further verification to assess its reliability.
- There may be a lack of experience on the part of the client with these types of transactions and, therefore, controls over existence may be nonexistent or poorly designed.
- The transactions may be complex in nature, making them difficult to understand.

.144 Management has a responsibility to design an internal control system that is responsive to the risk of existence of assets (in addition to the valuation of assets). As part of their risk assessment procedures, auditors need to assess those controls and determine if the controls have been implemented. Depending on the results of those assessments, the auditor should design an audit strategy that takes into consideration the entity's controls, including testing those controls, if those controls are to be relied upon and used as part of the auditor's audit evidence regarding the existence assertion. If the auditor's assessment indicates that management's design or operation of controls is not effective, then those deficiencies should be communicated to those charged with governance if the control deficiency is a significant deficiency or material weakness.

.145 Examples of procedures that can be performed by management that are designed to assess the existence of assets could include the following:

- Obtaining through site visits and documenting an understanding of existence controls placed in operation by any service organization that is utilized by the entity and periodically reassessing that understanding
- Obtaining evidence through direct testing or a SAS 70 type 2 report that the service organization's existence controls are appropriately designed and operating effectively
- Inspecting other documentation supporting the entity's interest in the security (for example, correspondence from the broker organization or trustee acknowledging transactions with the fund)

Communication With Those Charged With Governance

.146 In addition to instances in which communication with those charged with governance in other auditing sections is discussed, other select measures are outlined in AU section 380, *The Auditor's Communication With Those Charged With Governance* (AICPA, *Professional Standards*, vol. 1), that are specifically relevant during an economic crisis and when measuring fair value. AU section 380 establishes standards and provides guidance on the auditor's communication with those charged with governance. As noted in paragraph .05 of AU section 380, the auditor must communicate with those charged with governance matters related to the financial statement audit that are, in the auditor's professional judgment, significant and relevant to the responsibilities of those charged with governance in overseeing the financial reporting process. The auditor should communicate his or her views about the quality of the entity's significant accounting policies, accounting estimates, and financial statement disclosures.

.147 AU section 341 expands on the applicability of AU section 380, when the auditor has concluded that substantial doubt exists about the entity's ability to continue as a going concern. In that case, the auditor should communicate to those charged with governance the nature of the events or conditions identified, the possible effect on the financial statements, the sufficiency of the related disclosures, and the effects on the auditor's report.

Communicating Internal Control Related Matters Identified in an Audit

.148 In October 2008, the AICPA Auditing Standards Board (ASB) issued Statement on Auditing Standards (SAS) No. 115, *Communicating Internal Control Related Matters Identified in an Audit* (AICPA, *Professional Standards*, vol. 1, AU sec. 325). SAS No. 115 amends SAS No. 112, *Communicating Internal Control Related Matters Identified in an Audit* (AICPA, *Professional Standards*, vol. 1, AU sec. 325A), and further clarifies standards and provides guidance on communicating matters related to an entity's internal control over financial reporting (internal control) identified in an audit of financial statements.

.149 The new SAS is applicable whenever an auditor expresses an opinion on financial statements (including a disclaimer of opinion), except when the auditor is performing an integrated audit and will be expressing an opinion on the effectiveness of internal control over financial reporting under AT section 501, *An Examination of an Entity's Internal Control Over Financial Reporting That Is Integrated With an Audit of Its Financial Statements* (AICPA, *Professional Standards*, vol. 1). This new standard is effective for audits of financial statements for periods ending on or after December 15, 2009, with early implementation permitted.

.150 In general, SAS No. 115 retains many of the provisions of SAS No. 112; it provides guidance to (*a*) enhance the auditor's ability to identify and evaluate deficiencies in internal control during an audit, and then (*b*) communicate to management and those charged with governance those deficiencies that the auditor believes are significant deficiencies or material weaknesses.

.151 The key differences between SAS No. 115 and SAS No. 112 lie in the definitions of *material weaknesses* and *significant deficiencies*. Under SAS No. 112, the auditor applied criteria of likelihood and magnitude described in that standard to determine if a control deficiency reached the threshold of significant deficiency or material weakness. Under SAS No. 115, the same criteria are used; however, more judgment is allowed for in determining whether a control deficiency is a significant deficiency.

Definitions of Significant Deficiency *and* Material Weakness

.152 A *material weakness* is a deficiency, or combination of deficiencies, in internal control, such that a reasonable possibility exists that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. For the purpose of this definition, a reasonable possibility exists when the likelihood of the event is either *reasonably possible* or *probable* because those terms are used in FASB ASC 450-20-25-1 (originally, these terms appeared in FASB Statement No. 5, *Accounting for Contingencies*).[2]

.153 A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness yet important enough to merit attention by those charged with governance.

The Evaluation Process

.154 Although the auditor is not required to perform procedures specifically to identify deficiencies in internal control, during the course of the audit, the auditor may become aware of deficiencies in the design or operation of the entity's internal control. The auditor should evaluate the severity of each deficiency in internal control identified during the audit and determine whether the deficiency, individually or in combination with other deficiencies in internal control, rise to the level of significant deficiencies or material weaknesses. The severity of a deficiency in internal control depends on the following:

- The magnitude of the potential misstatement resulting from the deficiency or deficiencies
- Whether a reasonable possibility exists that the entity's controls will fail to prevent or to detect and correct a misstatement of an account balance or disclosure

.155 The severity of a deficiency does not depend on whether a misstatement actually occurred. If the auditor identifies a deficiency in internal control but has not identified an actual misstatement related to that deficiency, the auditor cannot automatically conclude that the deficiency is not a significant deficiency or a material weakness. If a misstatement has been identified, the auditor should consider the potential for further misstatement in the financial statements being audited.

---

[2] The term *reasonably possible* as used in the definition of the term *material weakness* has the same meaning as defined in Financial Accounting Standards Board (FASB) *Accounting Standards Codification* (ASC) 450-20-25-1:

> When a loss contingency exists, the likelihood that the future event or events will confirm the loss or impairment of an asset or the incurrence of a liability can range from probable to remote. This Statement uses the terms probable, reasonably possible, and remote to identify three areas within that range, as follows:
>
> *a.* *Probable.* The future event or events are likely to occur.
>
> *b.* *Reasonably possible.* The chance of the future event or events occurring is more than remote but less than likely.
>
> *c.* *Remote.* The chance of the future event or events occurring is slight.
>
> Therefore, the likelihood of an event is a *reasonable possibility* when it is reasonably possible or probable.

.156 The AICPA published Audit Risk Alert *Communicating Internal Control Related Matters in an Audit—Understanding SAS No. 115* (product no. 022539) to assist in understanding the requirements of this SAS. This Audit Risk Alert provides specific case studies to help determine whether identified control weaknesses would constitute a significant deficiency or material weakness; it can be obtained by calling the AICPA at (888) 777-7077 or visiting www.cpa2biz.com.

The Applicability of SAS No. 115 to Yellow Book and Single Audits

.157 The GAO has issued interim guidance on reporting on internal control over financial reporting, making it permissible for auditors to implement SAS No. 115 on their financial statement audits performed under *Government Auditing Standards*. For the full text of the GAO interim guidance related to SAS No. 115, go to www.gao.gov/govaud/icguidance0811.pdf. This guidance becomes effective concurrently with the auditor's implementation of SAS No. 115. However, OMB has not provided any guidance to date regarding use of the new guidance and definitions in SAS No. 115 for reporting on internal control over compliance in single audits. Therefore, it would not be appropriate for auditors to use definitions for reporting on internal control over compliance as found in SAS No. 115 until such time that OMB guidance is amended to allow usage of these new definitions. Readers should monitor the OMB Web site for further guidance at www.whitehouse.gov/omb and look to the Governmental Audit Quality Center Web site (www.aicpa.org/GAQC) for additional updates.

Withdrawal of GAAP Hierarchy From Auditing Standards

.158 In August 2009, the ASB voted to withdraw SAS No. 69, *The Meaning of* Present Fairly in Conformity With Generally Accepted Accounting Principles, as amended, from the auditing literature for nonissuers. This SAS was withdrawn as a result of recent pronouncements by FASB, Governmental Accounting Standards Board (GASB), and Federal Accounting Standards Advisory Board to incorporate their respective GAAP hierarchies into their respective authoritative literature.

.159 Interpretation No. 3, "The Auditor's Consideration of Management's Adoption of Accounting Principles for New Transactions or Events," of AU section 411, *The Meaning of* Present Fairly in Conformity With Generally Accepted Accounting Principles, also will be withdrawn automatically because the ASB did not direct that the interpretation be retained and moved elsewhere within the literature.

.160 The effective date of the withdrawal will be September 2009 to reflect the effective date of the FASB ASC, which is effective for financial statements for interim and annual periods ending after September 15, 2009.

.161 Further information about recent ASB projects and activities is available at www.aicpa.org/Professional+Resources/Accounting+and+Auditing/Audit+and+Attest+Standards/Auditing+Standards+Board/.

Accounting Issues and Developments

.162 Given the current economic crisis, auditors should consider a number of accounting and financial reporting issues, such as the following:

- Recent FASB pronouncements
- FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes—an interpretation of FASB Statement No. 109*
- Fair value, including fair value measurements in illiquid markets
- Impairment
- Liquidity restrictions
- Recent GASB pronouncements
- Tax exempt debt issues

Not-for-Profit Entities: Mergers and Acquisitions

.163 In May 2009, FASB issued FASB Statement No. 164, *Not-for-Profit Entities: Mergers and Acquisitions*.[3] This statement is effective for mergers occurring on or after December 15, 2009, and acquisitions for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2009. Earlier implementation is not permitted.

.164 The statement is intended to improve the relevance, representational faithfulness, and comparability of the information that a not-for-profit entity provides in its financial reports about a combination with one or more other not-for-profit entities, businesses, or nonprofit activities. To accomplish that, this statement establishes principles and requirements for how a not-for-profit entity

- determines whether a combination is a merger or an acquisition.
- applies the carryover method in accounting for a merger.
- applies the acquisition method in accounting for an acquisition, including determining which of the combining entities is the acquirer.
- determines what information to disclose to enable users of financial statements to evaluate the nature and financial effects of a merger or an acquisition.

.165 It also is intended to improve the information that a not-for-profit entity provides about goodwill and other intangible assets after an acquisition by amending FASB Statement No. 142, *Goodwill and Other Intangible Assets*, to make it fully applicable to not-for-profit entities. More information and the text of FASB Statement No. 164 can be found at www.fasb.org.

FASB Statement No. 168

.166 FASB Statement No. 168, as codified in FASB ASC 105, *Generally Accepted Accounting Principles*, is effective for financial statements issued for interim and annual periods ending after September 15, 2009. Nonpublic nongovernmental entities that have not previously followed the guidance included in TIS sections 5100.38–.76, "Revenue Recognition" (AICPA, *Technical Practice Aids*), which is now included in FASB ASC as authoritative should account for the adoption of that guidance as a change in accounting principle, on a prospective basis, for revenue arrangements entered into or materially modified in

[3] At the date of this writing, this guidance has not yet been included in FASB ASC. Readers are encouraged to visit the FASB ASC Web site at http://asc.fasb.org/home and monitor codification updates.

those fiscal years beginning on or after December 15, 2009, and interim periods within those years. If an accounting change results from the application of this guidance, an entity should disclose the nature and reason for the change in accounting principle in their financial statements. This new standard flattens the GAAP hierarchy to two levels: one that is authoritative (in FASB ASC) and one that is nonauthoritative (not in FASB ASC). Exceptions include all rules and interpretive releases of the SEC under the authority of federal securities laws, which are sources of authoritative GAAP for SEC registrants, and certain grandfathered guidance having an effective date before March 15, 1992. This statement creates FASB ASC 105.

.167 FASB Statement No. 168 is the final standard that will be issued by FASB in that form. It was added to FASB ASC through Accounting Standards Update (ASU) No. 2009-02 on June 30, 2009. No new standards in the form of statements, staff positions, Emerging Issues Task Force (EITF) abstracts, or AICPA accounting SOPs, for example, will be issued. Instead, FASB will issue ASUs. FASB will not consider ASUs as authoritative in their own right. Instead, they will serve only to update FASB ASC, provide background information about the guidance, and provide the basis for conclusions on changes made to FASB ASC.

FASB ASC

.168 On the effective date of FASB Statement No. 168, FASB ASC became the source of authoritative U.S. accounting and reporting standards for nongovernmental entities, in addition to guidance issued by the SEC. At that time, FASB ASC superseded all then-existing, non-SEC accounting and reporting standards for nongovernmental entities. Once effective, all other nongrandfathered, non-SEC accounting literature not included in FASB ASC became nonauthoritative. This change will affect accountants and auditors alike.

.169 FASB ASC is a major restructuring of accounting and reporting standards designed to simplify user access to all authoritative U.S. GAAP by providing the authoritative literature in a topically organized structure. FASB ASC disassembled and reassembled thousands of nongovernmental accounting pronouncements (including those of FASB, the EITF, and the AICPA) to organize them under approximately 90 topics. FASB ASC includes all accounting standards issued by a standard setter within levels A–D of the current U.S. GAAP hierarchy. FASB ASC also includes relevant portions of authoritative content issued by the SEC, as well as select SEC staff interpretations and administrative guidance issued by the SEC; however, FASB ASC is not the official source of SEC guidance and does not contain the entire population of SEC rules, regulations, interpretive releases, and staff guidance.

.170 FASB ASC is not intended to change U.S. GAAP or any requirements of the SEC; rather, it is part of FASB's efforts to reduce the complexity of accounting standards and also to facilitate international convergence. Moreover, FASB ASC does not include governmental accounting standards. The purposes behind the codification project include the following:

- Reduce the amount of time and effort required to solve an accounting research issue
- Mitigate the risk of noncompliance with standards through improved usability of the literature

- Provide accurate information with real-time updates as new standards are released
- Assist FASB with the research and convergence efforts required during the standard setting process
- Become the authoritative source of literature for the completed eXtensible Business Reporting Language (XBRL) taxonomy
- Clarify that guidance not contained in FASB ASC is not considered authoritative

.171 FASB ASC uses a topical structure in which guidance is organized into areas, topics, subtopics, sections, and subsections. These terms are defined as follows:

Areas. The broadest category in FASB ASC, which represents a grouping of topics.

Topics. The broadest categorization of related content, which correlates with the International Accounting Standards (IASs) and International Financial Reporting Standards (IFRSs).

Subtopics. Subsets of a topic, which are generally distinguished by type or scope.

Sections. Categorization of the content into such groups as recognition, measurement, or disclosure. The sections' structure correlates with the IASs and IFRS.

Subsections. Further segregation and navigation of content below the section level.

.172 Topics, subtopics, and sections are numerically referenced. This effectively organizes the content without regard to the original standard setter or standard from which the content was derived. An example of the numerical referencing is FASB ASC 305-10-05, in which *305* is the *Cash and Cash Equivalents* topic, *10* represents the "Overall" subtopic, and *05* represents the "Overview and Background" section. Constituents are encouraged to begin using FASB ASC, which can be accessed at http://asc.fasb.org/home. To read more about FASB ASC, including recent developments and updates, please see the AICPA's dedicated FASB ASC Web site at www.aicpa.org/Professional+Resources/Accounting+and+Auditing/FASB+Accounting+Standards+Codification/.

Consolidation of Variable Interest Entities

.173 In June 2009, FASB issued FASB Statement No. 167, *Amendments to FASB Interpretation No. 46(R)*,[4] which changes how a company determines when an entity that is insufficiently capitalized or is not controlled through voting (or similar rights) should be consolidated. The determination of whether a company is required to consolidate an entity is based on, among other things, an entity's purpose and design and a company's ability to direct the activities of the entity that most significantly affect the entity's economic performance.

.174 This statement also amends FASB Interpretation No. 46 (revised December 2003), *Consolidation of Variable Interest Entities—an interpretation of*

[4] See footnote 3.

ARB No. 51 (codified primarily at FASB ASC 810-10), to eliminate the quantitative approach previously required for determining the primary beneficiary of a variable interest entity, which was based on determining which enterprise absorbs the majority of the entity's expected losses, receives a majority of the entity's expected residual returns, or both.

.175 Entities will be required to provide additional disclosures about involvement with variable interest entities and any significant changes in risk exposure due to that involvement. Entities also will be required to disclose how involvement with a variable interest entity affects the entity's financial statements.

.176 FASB Statement No. 167 retains the scope of FASB Interpretation No. 46(R) with the addition of entities previously considered qualifying special purpose entities because the concept of these entities was eliminated in FASB Statement No. 166, *Accounting for Transfers of Financial Assets—an amendment of FASB Statement No. 140*.

.177 This statement is effective as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period, and for interim and annual reporting periods thereafter. Earlier application is prohibited.

Accounting for Transfers of Financial Assets

.178 Also in June 2009, FASB issued FASB Statement No. 166,[5] which is a revision to FASB Statement No. 140, *Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities—a replacement of FASB Statement No. 125* (which was codified in FASB ASC 860, *Transfers and Servicing*), and will require more information about transfers of financial assets, including securitization transactions, and where entities have continuing exposure to the risks related to transferred financial assets. It eliminates the concept of a qualifying special purpose entity, changes the requirements for derecognizing financial assets, and requires additional disclosures. The purpose of this statement is to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor's continuing involvement, if any, in transferred financial assets.

.179 Additionally, on and after the effective date, the concept of a qualifying special purpose entity is no longer relevant for accounting purposes. Therefore, formerly qualifying special purpose entities (as defined under previous accounting standards) should be evaluated for consolidation by reporting entities on and after the effective date in accordance with the applicable consolidation guidance.

.180 FASB Statement No. 166 must be applied as of the beginning of each reporting entity's first annual reporting period that begins after November 15, 2009, for interim periods within that first annual reporting period and for interim and annual reporting periods thereafter. Earlier application is prohibited. This statement must be applied to transfers occurring on or after the effective date; however, the disclosure provisions should be applied to transfers that occurred both before and after the effective date.

---

[5] See footnote 3.

Subsequent Events

.181 In May 2009, FASB issued FASB Statement No. 165, *Subsequent Events*, which has been codified at FASB ASC 855, *Subsequent Events*, and which is effective for interim and annual periods ending after June 15, 2009. This statement is intended to establish general standards of accounting for and disclosure of events that occur after the balance sheet date but before financial statements are issued or are available to be issued. It requires the disclosure of the date through which an entity has evaluated subsequent events and the basis for that date (that is, whether that date represents the date the financial statements were issued or were available to be issued). The purpose of this disclosure is to alert all users of financial statements that an entity has not evaluated subsequent events after that date in the set of financial statements being presented.

.182 In particular, this statement sets forth the following:

- The period after the balance sheet date during which management of a reporting entity should evaluate events or transactions that may occur for potential recognition or disclosure in the financial statements
- The circumstances under which an entity should recognize events or transactions occurring after the balance sheet date in its financial statements
- The disclosures that an entity should make about events or transactions that occurred after the balance sheet date

.183 FASB states that this statement should not result in significant changes in current practice with regard to the subsequent events that an entity reports, either through recognition or disclosure, in its financial statements. The full text of FASB Statement No. 165 can be found online at www.fasb.org; the codified version is at FASB ASC 855.

FASB Interpretation No. 48

.184 FASB Interpretation No. 48, (which is codified at FASB ASC 740, *Income Taxes*), was issued in June 2006 and is effective for fiscal years beginning after December 15, 2006. However, subsequent to its issuance, FASB issued FSP FIN 48-2, *Effective Date of FASB Interpretation No. 48 for Certain Nonpublic Enterprises*, and FSP FIN 48-3, *Effective Date of FASB Interpretation No. 48 for Certain Nonpublic Enterprises* (which is also codified at FASB ASC 740, *Income Taxes*), which defer the effective date of FASB Interpretation No. 48 for nonpublic enterprises, as defined in the FASB ASC glossary, and included in the FSP's scope, to the annual financial statements for fiscal years beginning after December 15, 2008. For the full text of FASB Interpretation No. 48 and its associated FSPs, visit the FASB Web site at www.fasb.org.

.185 FASB ASC 740-10-25-6 states that financial statement tax accrual may only contain positions that meet the "more-likely-than-not" standard, and any variances must be disclosed in the financial statements. This translates to more work for accountants and auditors on the tax accrual, as you evaluate even garden-variety issues such as unreasonable compensation or expensing versus capitalization. It also means that positions taken on the return (or that were taken in any open year) that do not meet the more-likely-than-not standard will be disclosed and will likely be subject to increased IRS scrutiny.

.186 The evaluation of a tax position in accordance with this interpretation is a two-step process. The first step is recognition: The enterprise determines whether it is more likely than not that a tax position will be sustained upon examination, including resolution of any related appeals or litigation processes, based on the technical merits of the position. In evaluating whether a tax position has met the more-likely-than-not recognition threshold, the enterprise should presume that the position will be examined by the appropriate taxing authority that would have full knowledge of all relevant information. The second step is measurement: A tax position that meets the more-likely-than-not recognition threshold is measured to determine the amount of benefit to recognize in the financial statements. The tax position is measured at the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement.

.187 Tax positions that previously failed to meet the more-likely-than-not recognition threshold should be recognized in the first subsequent financial reporting period in which that threshold is met. Previously recognized tax positions that no longer meet the more-likely-than-not recognition threshold should be derecognized in the first subsequent financial reporting period in which that threshold is no longer met. Use of a valuation allowance, as described in the FASB ASC glossary, is not an appropriate substitute for the derecognition of a tax position. The requirement to assess the need for a valuation allowance for deferred tax assets based on the sufficiency of future taxable income is unchanged by this interpretation.

.188 A practice guide for accountants, auditors, and tax advisers has been posted to the AICPA's Tax Center at http://tax.aicpa.org/Resources/Professional+Standards+and+Ethics/Practice+Guide+on+Accounting+for+Uncertain+Tax+Positions+Under+FIN+48.htm. Also, an AICPA continuing professional education (CPE) course on accounting for income taxes that has been updated for FASB Interpretation No. 48 is now available. Please visit www.cpa2biz.com for more information on these products.

Additional Implementation Guidance for FASB Interpretation No. 48

.189 In September 2009, FASB released ASU 2009-6, *Implementation Guidance on Accounting for Uncertainty in Income Taxes and Disclosure Amendments for Nonpublic Entities*, which clarifies and provides examples of the application of FASB Interpretation No. 48 to not-for-profit entities and pass-through entities, such as S corporations or partnerships, and modifies the required financial statement disclosures for nonpublic entities.

.190 Among the points addressed in the ASU is that managements' determination of the taxable status as a pass-through entity or tax-exempt NFP, is a tax position subject to the standards required for accounting for uncertainty in income taxes in FASB ASC 740, *Income Taxes*.

.191 Additionally, this ASU eliminates for nonpublic entities the disclosures required by both FASB ASC 740-10-50-15(a), which requires a tabular reconciliation of the total amount of unrecognized tax benefits at the beginning and end of the periods presented, and FASB ASC 740-10-50-15(b), which requires the disclosure of the total amount of unrecognized tax benefits that, if recognized, would affect the effective tax rate.

.192 This ASU is effective for financial statements issued for interim and annual periods ending after September 15, 2009 for entities that have begun applying the standards for accounting for uncertainty in income taxes. For those entities that have deferred the application of those standards in accordance with FASB ASC 740-10-65-1(e), the amendments are effective upon adoption of those standards. Readers can find the full text of this ASU at www.fasb.org.

Fair Value

.193 Among the causes cited for the economic crisis, the guidance in FASB ASC 820 (formerly FASB Statement No. 157) has received a great deal of attention. FASB ASC 820-10-20 defines *fair value* and establishes a framework for measuring fair value; however, it does not dictate when an entity must measure something at fair value, nor does it expand the use of fair value in any way. The need to understand fair value accounting has increased in importance as alternative investments increased in popularity and complexity.

.194 This guidance defines *fair value* as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date." A contention with this guidance is the difficulty of applying the existing guidance in an illiquid or distressed market, such as the current one. This difficulty has the potential to allow inconsistencies in application by accountants and auditors. Prior to the issuance of FASB Staff Position (FSP) FAS 157-4, *Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly,* which is codified at FASB ASC 820-10, the areas of fair value guidance that related to measuring fair value in an illiquid market were limited to the following mentions:

- "An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets or liabilities; it is not a forced transaction (for example, a forced liquidation or distress sale)."
- "Market participants are buyers and sellers in the principal (or most advantageous) market for the asset or liability that are ... [w]illing to transact for the asset or liability; that is, they are motivated but not forced or otherwise compelled to do so."
- "For example, a transaction price might not represent the fair value of an asset or liability at initial recognition if . . . [t]he transaction occurs under duress or the seller is forced to accept the price in the transaction. For example, that might be the case if the seller is experiencing financial difficulty."

.195 Both the SEC and FASB took notice of constituents' desire for further guidance. In September 2008, the SEC issued *SEC Office of the Chief Accountant and FASB Staff Clarifications on Fair Value Accounting* to provide immediate clarifications on fair value in illiquid markets for preparers and auditors until FASB was able to provide additional interpretative guidance.

Determining Whether a Market Is Not Active and a Transaction Is Not Distressed

.196 On April 9, 2009, FASB issued FSP FAS 157-4, which is codified at FASB ASC 820-10. The purpose of this FSP is to provide additional guidance in the application of fair value accounting in an inactive market; it supersedes FSP

FAS 157-3, *Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active*. Among other points, the new guidance

- affirms that the objective of fair value when the market for an asset is not active is the price that would be received to sell the asset in an orderly transaction (that is, not a forced liquidation or distressed sale) between market participants at the measurement date under current market conditions (that is, in the inactive market).
- clarifies and includes additional factors for determining whether there has been a significant decrease in market activity for an asset when the market for that asset is not active.
- eliminates the proposed presumption that all transactions are distressed (not orderly) unless proven otherwise. This guidance instead will require an entity to base its conclusion about whether a transaction was not orderly on the weight of the evidence.
- includes an example that provides additional explanation on estimating fair value when the market activity for an asset has declined significantly.
- requires an entity to disclose a change in valuation technique (and the related inputs) resulting from the application of this guidance and to quantify its effects, if practicable, by major category.
- applies to all fair value measurements when appropriate.

.197 This new guidance is effective for interim and annual reporting periods ending after June 15, 2009, and shall be applied prospectively. Early adoption is permitted for periods ending after March 15, 2009. Earlier adoption for periods ending before March 15, 2009, is not permitted. If a reporting entity elects to adopt early either FSP FAS 115-2 and FAS 124-2, *Recognition and Presentation of Other-Than-Temporary Impairments*, which was primarily codified in FASB ASC 310-55, 325-40, and 320-10, or FSP FAS 107-1 and APB 28-1, *Interim Disclosures about Fair Value of Financial Instruments*, which has been codified at FASB ASC 270-10-50-1, 320-10, and 825-10-50, the reporting entity also is required to adopt this FSP early. Additionally, if the reporting entity elects to adopt early, FSP FAS 115-2 and FAS 124-2 also must be adopted early. This FSP does not require disclosures for earlier periods presented for comparative purposes at initial adoption. In periods after initial adoption, this FSP requires comparative disclosures only for periods ending after initial adoption.

Interim Disclosures About Fair Value of Financial Instruments

.198 On April 9, 2009, FASB released FSP FAS 107-1 and APB 28-1, which has been codified at FASB ASC 270-10-50-1, 320-10, and 825-10-50. This guidance relates to fair value disclosures for any financial instruments that are not currently reflected on the balance sheet of companies at fair value. Prior to this issuance, fair values for these assets and liabilities were disclosed only once a year. The guidance requires these disclosures to be made on a quarterly basis, providing qualitative and quantitative information about fair value estimates for all those financial instruments not measured on the balance sheet at fair value. The guidance

- applies to all financial instruments as defined by the FASB ASC glossary and discussed in FASB ASC 825-10-50-8.

P1: G.Shankar
ACPA108-01 ACPA108.cls September 29, 2009 15:31

- applies to the financial statements of publicly traded companies, as defined in the FASB ASC glossary, for interim and annual reporting periods.
- requires an entity to disclose the methods and significant assumptions used to estimate the fair value of financial instruments and shall describe changes in methods and significant assumptions, if any, during the period.

.199 This guidance is effective for interim reporting periods ending after June 15, 2009, with early adoption permitted for periods ending after March 15, 2009. An entity may adopt early only if it also elects to adopt early FSP FAS 157-4 and FSP FAS 115-2 and FAS 124-2. This FSP does not require disclosures for earlier periods presented for comparative purposes at initial adoption. In periods after initial adoption, this FSP requires comparative disclosures only for periods ending after initial adoption.

Measuring Liabilities at Fair Value

.200 On August 27, 2009, FASB issued ASU No. 2009-05, *Measuring Liabilities at Fair Value*. This ASU was issued to increase the consistency in the application of FASB ASC 820 to liabilities because many constituents had expressed concern. This ASU applies to all entities that measure liabilities at fair value under FASB ASC 820 and amends sections of FASB ASC 820-10.

.201 This ASU states that, in circumstances in which a quoted price in an active market for the identical liability is not available, fair value of the liability must be measured by either (*a*) a valuation technique that uses the quoted price of the identical liability when traded as an asset or quoted prices for similar liabilities or similar liabilities when traded as assets, or (*b*) another valuation technique that is consistent with the principles of FASB ASC 820, such as an income approach or a market approach. Further, if a restriction on the transference of the liability exists, the ASU clarifies that an entity is not required to factor that in to the inputs of the fair value determination. Lastly, the ASU also clarifies that a quoted price in an active market for the identical liability, or an unadjusted quoted price in an active market for the identical liability, when traded as an asset, are level 1 measurements within the fair value hierarchy. The guidance in this ASU is effective for the first reporting period (including interim periods) beginning after issuance. The full text of the ASU can be accessed from FASB's Web site at www.fasb.org.

Other-Than-Temporary Impairment

.202 Determining when an investment is other-than-temporarily impaired is another topic that has received increased attention in today's economic environment. FSP FAS 115-1 and FAS 124-1, *The Meaning of* Other-Than-Temporary Impairment *and Its Application to Certain Investments*, as amended by FSP FAS 115-2 and FAS 124-2, is codified in several topics in FASB ASC, including FASB ASC 320, *Investments—Debt and Equity Securities*, and FASB ASC 325, *Investments—Other*. This guidance addresses the determination of when an investment is considered impaired, whether the impairment is other-than-temporary, and the measurement of the impairment loss. Also included in this amended guidance are accounting issues to be considered subsequent to the recognition of other-than-temporary impairments and related disclosures about unrealized losses as a result of the other-than-temporary impairment. This amended guidance applies to (*a*) debt and equity securities within the scope of FASB ASC 320; (*b*) debt and equity securities within the scope of FASB ASC 958320 that are held by an investor that reports a performance indicator; and (*c*) equity securities not within the scope of FASB ASC 320 and 958-320 and not accounted for under the equity method, pursuant to FASB ASC 323, *Investments—Equity Method and Joint Ventures*. The auditor also should be alert for all types of assets that can become impaired, including goodwill, deferred tax assets, and real property. Given the current economic situation, entities should be alert to values of many types of assets on the balance sheet and possible impairment issues. Readers should consult the appropriate accounting requirements for further information. For the full text of FSP FAS 115-1 and FAS 124-1, as amended, please visit the FASB Web site at www.fasb.org.

Recognition and Presentation of Other-Than-Temporary Impairments

.203 On April 9, 2009, FASB released FSP FAS 115-2 and FAS 124-2, which was primarily codified at FASB ASC 310-30, 320-10, and 325-40. The purpose of this FSP is to bring greater consistency to the timing of impairment recognition and provide greater clarity to investors about the credit and noncredit components of impaired debt securities that are not expected to be sold. Among other points, the FSP

- limits its changes to existing guidance for determining whether an impairment is other than temporary to debt securities.
- replaces the existing requirement that the entity's management assert that it has both the intent and ability to hold an impaired security until recovery, with a requirement that management assert that it does not have the intent to sell the security, or it is more-likely-than-not it will not have to sell the security before recovery of its costs basis.
- incorporates examples of factors from existing literature that should be considered in determining whether a debt security is other-than-temporarily impaired and how those factors interact with the requirement to assert that the entity does not intend to sell the security, and it is more-likely-than-not that the entity will not have to sell the security before recovery of its cost basis.
- requires an entity to recognize the credit component of an other-than-temporary impairment of a debt security in earnings and the remaining portion in other comprehensive income, when an entity does not intend to sell the security, and it is more-likely-than-not that the entity will not have to sell the security before recovery of its cost basis.
- requires an entity to recognize noncredit losses on held-to-maturity debt securities in other comprehensive income and amortize that amount over the remaining life of the security with no effect on earnings, unless the security is subsequently sold, or additional credit losses exist.
- includes guidance for debt securities accounted for in accordance with FASB ASC 310-30, stipulating that credit losses should be measured on the basis of an entity's estimate of the decrease in expected cash flows, including those that result from an increase in expected prepayments.
- clarifies that existing premiums or discounts and subsequent changes in estimated cash flows or fair value should continue to be

accounted for in accordance with existing guidance (for example, EITF Issue No. 99-20, "Recognition of Interest Income and Impairment on Purchased Beneficial Interests and Beneficial Interests That Continue to Be Held by a Transferor in Securitized Financial Assets," which was primarily codified at FASB ASC 325-40).

- requires an entity to present the total other-than-temporary impairment in the statement of earnings, with an offset for the amount recognized in other comprehensive income.
- requires an entity to present separately in the financial statement where the components of accumulated other comprehensive income are reported and amounts recognized therein related to held-to-maturity and available-for-sale debt securities, for which a portion of an other-than-temporary impairment has been recognized in earnings
- modifies the disclosure requirements of certain debt and equity securities to require an entity to provide the following:
    — The cost basis of available-for-sale and held-to-maturity debt securities by major security type
    — The methodology and key inputs, such as performance indicators of the underlying assets in the security, loan to collateral value ratios, third-party guarantees, levels of subordination, and vintage, used to measure the portion of an other-than-temporary impairment related to credit losses by major security type
    — A tabular rollforward of the amount related to credit losses recognized in earnings for debt securities.
- modifies previous guidance to require that major security classes be based on the nature and risks of the security and additional types of securities to be included in the list of major security types listed in FASB ASC 942-320-50-2.
- requires the preceding additional disclosures, as well as all prior existing disclosures, for interim periods

.204 The guidance is effective for interim and annual reporting periods ending after June 15, 2009, with early adoption permitted for periods ending after March 15, 2009. Earlier adoption for periods ending before March 15, 2009, is not permitted. As discussed previously, if an entity elects to adopt early either FSP FAS 157-4 or FSP FAS 107-1 and APB 28-1, the entity also is required to adopt this FSP early. Additionally, if an entity elects to adopt this FSP early, it is required to adopt FSP FAS 157-4. This FSP does not require disclosures for earlier periods presented for comparative purposes at initial adoption. In periods after initial adoption, this FSP requires comparative disclosures only for periods ending after initial adoption. More information is available at www.fasb.org.

NFP Consolidations and Equity Method Guidance

.205 In May 2008, FASB issued FSP SOP 94-3-1 and AAG HCO-1, *Omnibus Changes to Consolidation and Equity Method Guidance for Not-for-Profit Organizations* (codified at FASB ASC 958-810). This FSP changes the guidance on consolidation and the equity method of accounting in SOP 94-3, *Reporting of Related Entities by Not-for-Profit Organizations* (AICPA, *Technical Practice*

Aids, ACC sec. 10,610), and the AICPA Audit and Accounting Guide *Health Care Entities* (guide). The FSP

- eliminates the temporary control exception to consolidation that currently exists for certain relationships between NFPs, amends the definition of majority voting interest in the board of another entity in SOP 94-3 and the guide, and conforms the categorization of sole corporate membership in SOP 94-3 to that in the guide;
- confirms the continued applicability to NFPs of the consensus guidance on consolidation of special purpose entity lessors in EITF Issue No. 90-15, "Impact of Nonsubstantive Lessors Residual Value Guarantees, and Other Provisions in Leasing Transaction," No. 96-21, "Implementing Issues in Accounting for Leasing Transactions involving Special Purpose Entities," and No. 97-1 "Implementation Issues in Accounting for Lease Transactions, including Those involving Special-Purpose Entities;"
- requires that NFPs apply the guidance in
    - — SOP 78-9, *Accounting for Investments in Real Estate Ventures* (AICPA, *Technical Practice Aids*, ACC sec. 10,240), on the equity method of accounting to their noncontrolling interests in for-profit real estate partnerships, limited liability companies (LLCs), and similar entities unless those investments are reported at fair value, where permitted,
    - — FSP SOP 78-9-1, *Interaction of AICPA Statement of Position 78-9 and EITF Issue No. 04-5*, to help determine whether their interests in for-profit partnerships, LLCs, and similar entities are controlling interests or noncontrolling interests,
    - — EITF Issue No. 03-16, "Accounting for Investments in Limited Liability Companies," to determine whether an LLC should be viewed as similar to a partnership, as opposed to a corporation, for purposes of determining whether noncontrolling interests in an LLC or a similar entity should be accounted for in accordance with SOP 78-9 and related guidance.

.206 This FSP is effective for fiscal years beginning after June 15, 2008. More information and the full text of the FSP are available at www.fasb.org.

Accounting for Losses Due to Fraud

.207 A topic of discussion for management and their auditors is the manner in which losses due to fraud are reflected in the financial statements. Because no accounting standard exists that provides specific guidance on accounting for losses due to fraud, application of professional judgment in this matter can lead to different results. For example, some entities have determined that the losses should be reported in the current period, when the entity became aware of the fraud, whereas others are opting for a restatement of the financial statements for one or more prior periods because they believe the loss in value occurred in a prior period and, therefore, an adjustment is appropriate. It is important that the auditor understand how the decision was reached and that proper disclosure be made in the financial statements.

.208 Auditors also may consider whether management has properly disclosed or recognized any liability associated with the potential clawback of distributions received from the perpetrator of Ponzi schemes. In the case of Bernard Madoff Investment Securities, a possibility exists that the bankruptcy trustee may file lawsuits to recover funds distributed to investors prior to the discovery of the fraud for the purpose of redistributing the funds. Management, in conjunction with appropriate legal counsel, should determine the probability and result of such a lawsuit and disclose or accrue a potential liability, as required by FASB ASC 450, *Contingencies*.

Liquidity Restrictions

.209 As discussed in the "Audit and Attestation Issues and Developments" section of this alert, TIS section 1100.15 addresses the potential accounting and auditing implications when a fund or its trustee imposes restrictions on a nongovernmental entity's ability to withdraw its balance in a money market fund or other short-term investment vehicle.

Recently Issued GASB Pronouncements and Related Guidance

.210 The following summaries are for informational purposes only and should not be relied upon as a substitute for a complete reading of the applicable standard.

GASB Statement No. 56, *Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards*

.211 GASB Statement No. 56, issued in March 2009, incorporates into GASB authoritative literature certain accounting and financial reporting guidance presented in the AICPA's SASs. This statement addresses three issues not included in the GASB authoritative accounting literature that establishes accounting principles—related party transactions, going concern considerations, and subsequent events.

.212 Although not intended to change practice, certain provisions of GASB Statement No. 56 differ from the AU sections of AICPA *Professional Standards* from which they were derived. For example, GASB Statement No. 56 specifies an evaluation by management of a government's ability to continue as a going concern for a period of 12 months beyond the financial statement date plus any period shortly thereafter about which a current doubt exists. Paragraph .03 of AU section 341 specifies that the auditor should evaluate whether substantial doubt exists about the entity's ability to continue as a going concern for a reasonable period of time.

.213 Other sections of AICPA *Professional Standards* that are incorporated into this statement are AU section 334, *Related Parties* (AICPA, *Professional Standards*, vol. 1), and AU section 560. GASB Statement No. 56 became effective upon issuance.

GASB Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*

.214 GASB Statement No. 55, issued in March 2009, incorporates the hierarchy GAAP for state and local governments into GASB authoritative literature. It is intended to make it easier for preparers of state and local government financial statements to identify and apply the GAAP hierarchy, which consists of sources of accounting principles used in the preparation of financial statements so that they are presented in conformity with GAAP and the framework for selecting those principles. Like GASB Statement No. 56, this statement contributes to GASB's efforts to codify all GAAP for state and local governments so that they derive from a single source.

.215 Prior to the statement, the GAAP hierarchy was set forth in SAS No. 69, *The Meaning of* Present Fairly in Conformity With Generally Accepted Accounting Principles, rather than in the authoritative accounting literature of GASB. GASB Statement No. 55 moves relevant portions of that SAS to GASB literature without substantive changes. GASB does not anticipate that this statement will result in a change in current practice. GASB Statement No. 55 became effective upon issuance.

GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*

.216 GASB Statement No. 54, issued in March 2009, initially distinguishes fund balance between amounts that are considered nonspendable, such as fund balance associated with inventories, and other amounts that are classified as spendable based on the relative strength of the constraints that control the purposes for which specific amounts can be spent. Beginning with the most binding constraints, fund balance amounts will be reported in the following classifications:

Restricted. Amounts that can be spent only for the specific purposes stipulated by constitution, external resource providers, or through enabling legislation.

Committed. Amounts that can be used only for the specific purposes determined by a formal action of the government's highest level of decision-making authority.

Assigned. Amounts intended to be used by the government for specific purposes but do not meet the criteria to be classified as restricted or committed.

Unassigned. The residual classification for the government's general fund and includes all spendable amounts not contained in the other classifications.

.217 The new standards also clarify the definitions of individual governmental fund types. It interprets certain terms within the definition of special revenue fund types, while further clarifying the debt service and capital projects fund type definitions. The final standard also specifies how economic stabilization or "rainy day" amounts should be reported. Because of the specific nature of these types of accounts, the statement considers stabilization amounts as specific purposes. Stabilization amounts should be reported in the general fund as restricted or committed if they meet the appropriate criteria. Only if the resources in the stabilization arrangement derive from a restricted or committed revenue source could a stabilization fund be reported as a special revenue fund.

.218 The definitions of the general fund, special revenue fund type, capital projects fund type, debt service fund type, and permanent fund type are clarified by the statement. The capital projects fund type was clarified for better alignment with the needs of preparers and users. Definitions are as follows:

General fund. Account for and report all financial resources and uses not accounted for and reported in another fund.

Special revenue funds. Account for and report the proceeds of specific revenue sources that are restricted or committed to expenditure for specified purposes other than debt service or capital projects.

Capital projects funds. Account for and report financial resources that are restricted, committed, or assigned to the expenditure for capital outlays, including the acquisition of construction of capital facilities and other capital assets.

Debt service funds. Account for and report financial resources that are restricted, committed, or assigned to expenditure for principal and interest.

Permanent funds. Account for and report resources that are restricted to the extent that only earnings, and not principal, may be used for purposes that support the reporting government's programs, that is, for the benefit of the government or its citizenry.

.219 For governments that use encumbrance accounting, significant encumbrances should be disclosed in the notes to the basic financial statements by major funds in the aggregate in conjunction with disclosures about other significant commitments. They should not be separately displayed within committed, assigned, or restricted categories.

.220 GASB Statement No. 54 is effective for financial statements for periods beginning after June 15, 2010. Earlier application is encouraged. Fund balance reclassifications made to conform to GASB Statement No. 54 should be retroactively applied by restating fund balance for all prior periods presented.

GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*

.221 GASB Statement No. 53, issued in June 2008, addresses the recognition, measurement, and disclosure of information regarding derivative instruments entered into by state and local governments. Derivative instruments are often complex financial arrangements used by governments to manage specific risks or to make investments. By entering into these arrangements, governments receive and make payments based on market prices without actually entering into the related financial or commodity transactions. Derivative instruments associated with changing financial and commodity prices result in changing cash flows and fair values that can be used as effective risk management or investment tools. Derivative instruments, however, also can expose governments to significant risks and liabilities. Common types of derivative instruments used by governments include interest rate and commodity swaps, interest rate locks, options (caps, floors, and collars), swaptions, forward contracts, and futures contracts.

.222 Governments enter into derivative instruments as investments; as hedges of identified financial risks associated with assets or liabilities or expected transactions (that is, hedgeable items); or to lower the costs of borrowings. Governments often enter into derivative instruments with the intention of effectively fixing cash flows or synthetically fixing prices. For example, a government with variable rate debt may enter into a derivative instrument designed to synthetically fix the debt's interest rate, thereby hedging the risk that rising interest rates will negatively affect cash flows. Governments also enter into derivative instruments to offset the changes in fair value of hedgeable items.

.223 A key provision in this statement is that derivative instruments covered in its scope, with the exception of synthetic guaranteed investment contracts that are fully benefit-responsive, are reported at fair value. For many derivative instruments, historical prices are zero because their terms are developed so that the instruments may be entered into without a payment being received or made. The changes in fair value of derivative instruments that are used for investment purposes or that are reported as investment derivative instruments because of ineffectiveness are reported within the investment revenue classification. Alternatively, the changes in fair value of derivative instruments that are classified as hedging derivative instruments are reported in the statement of net assets as deferrals.

.224 Derivative instruments associated with hedgeable items that are determined to be effective in reducing exposures to identified financial risks are considered hedging derivative instruments. Effectiveness is determined by considering whether the changes in cash flows or fair values of the potential hedging derivative instrument substantially offset the changes in cash flows or fair values of the hedgeable item. In these instances, hedge accounting should be applied. Under hedge accounting, the changes in fair values of the hedging derivative instrument are reported as either deferred inflows or deferred outflows in a government's statement of net assets.

.225 GASB Statement No. 53 describes the methods of evaluating effectiveness. The consistent critical terms method considers the terms of the potential hedging derivative instrument and the hedgeable item. If relevant terms match, or in certain instances, are similar, a potential hedging derivative instrument is determined to be effective. The other methods are based on quantitative analyses. The synthetic instrument method considers whether a fixed rate or price has been established within a prescribed range. The dollar-offset method evaluates changes in expected cash flows or fair values over time between the potential hedging derivative instrument and the hedgeable item. The regression analysis method considers the relationship between changes in the cash flows or fair values of the potential hedging derivative instrument and the hedgeable item. In these methods, critical and quantitative values are evaluated to determine whether a potential hedging derivative instrument is effective. Quantitative methods other than those specified in the statement are permitted, provided that they address whether the changes in cash flows or fair values of the potential hedging derivative instrument substantially offset the changes in cash flows or fair values of the hedgeable item.

.226 The disclosures previously required by GASB Technical Bulletin (TB) No. 2003-1, *Disclosure Requirements for Derivatives Not Reported at Fair Value on the Statement of Net Assets*, have been incorporated into GASB Statement No. 53 and, therefore, GASB TB 2003-1 is superseded upon implementation of GASB Statement No. 53. The objectives, terms, and risks of hedging derivative instruments are required disclosures. Disclosures also include a summary of derivative instrument activity that provides an indication of the location of fair value amounts reported on the financial statements. The disclosures for investment derivative instruments are similar to the disclosures of other investments.

.227 GASB Statement No. 53 is effective for financial statements for periods beginning after June 15, 2009. Earlier application is encouraged. For potential hedging derivative instruments existing prior to the fiscal period during which this statement is implemented, the evaluation of effectiveness should be performed as of the end of the current period. If determined to be effective, hedging derivative instruments are reported as if they were effective from their inception. If determined to be ineffective, the potential hedging derivative instrument is then evaluated as of the end of the prior reporting period. A comprehensive implementation guide to GASB Statement No. 53 was released by GASB in April 2009.

GASB TB 2008-1, *Determining the Annual Required Contribution Adjustment for Postemployment Benefits*

.228 GASB TB 2008-1 clarifies the requirements of GASB Statement Nos. 27 and 45 for calculating the annual required contribution (ARC) adjustment. GASB TB 2008-1 applies to situations in which the actuarial valuation separately identifies the actual amount that is included in the ARC related to the amortization of past employer contribution deficiencies or excess contributions to a pension or other postemployment benefits (OPEB) plan. In response to constituent feedback that questioned the availability of actual amounts, GASB Statement Nos. 27 and 45 required a procedure for estimating the amount. GASB TB 2008-1 encourages use of the actual amount, if known, in place of the estimation procedure for purposes of the ARC adjustment.

.229 With regard to pensions, the provisions of GASB TB 2008-1 are effective for financial statements for periods ending after December 15, 2008. With regard to OPEB, the provisions of GASB TB 2008-1 are effective for financial statements for periods ending after December 15, 2008, or simultaneously with the initial implementation of GASB Statement No. 45, whichever is later.

GASB Concepts Statement No. 5, *Service Efforts and Accomplishments Reporting—an amendment of GASB Concepts Statement No. 2*

.230 GASB Concepts Statement No. 5, issued in November 2008, updates provisions in GASB Concepts Statement No. 2 in order to reflect developments that have occurred since GASB Concepts Statement No. 2 was issued in 1994. The proposed changes are based on the findings of extensive research by GASB and others and the results of GASB monitoring of state and local governments that have been using and reporting service efforts and accomplishments (SEA) performance information.

.231 The revisions to GASB Concepts Statement No. 2 clarify that it is beyond the scope of GASB to establish the goals and objectives of state and local government services, to develop specific nonfinancial measures or indicators of service performance, or to set benchmarks for service performance. To emphasize this point, GASB Concepts Statement No. 5 removes the entire section of Concepts Statement No. 2, "Developing Reporting Standards for SEA Information." GASB Concepts Statement No. 2 also was amended to update terminology and to modify certain provisions to reflect what has taken place over the past 14 years.

Tax Exempt Bonds—Accounting and Auditing Considerations in the Current Environment

.232 The current credit environment has affected the market for debt securities. For example, several entities that insure tax exempt debt have been downgraded by rating agencies, and some investors have avoided certain debt securities. Although each situation is different and should be evaluated based on its own specific facts and circumstances, the current situation may raise various accounting and auditing issues pertaining to tax exempt debt, including, but not limited to, the following:

- Bond restructurings
- Derivative and hedge accounting implications
- Potential violation of debt covenants
- Classification of the debt on the balance sheet as either a current or noncurrent liability
- Subsequent event disclosures
- Going concern issues

.233 An ad hoc AICPA member task force developed a nonauthoritative article to address these issues in more detail. This article can be found at www.aicpa.org/download/acctstd/ARS_article14.pdf.

Convergence With IFRSs

.234 Since the signing of the Norwalk Agreement by FASB and the International Accounting Standards Board (IASB), the bodies have had a common goal—one set of accounting standards for international use. In this agreement, each body acknowledged its commitment to the development of high quality, compatible accounting standards that could be used for both domestic and cross-border financial reporting. FASB and the IASB have undertaken several joint projects, which are being conducted simultaneously in a coordinated manner to further the goal of convergence of U.S. GAAP and IFRS. These ongoing joint projects address the conceptual framework, business combinations, financial statement presentation, and revenue recognition. The "On the Horizon" section of this alert discusses these joint projects. For more information, visit www.fasb.org and www.iasb.org.

IFRS Roadmap

.235 In August 2008, the SEC voted to publish for public comment a proposed roadmap that could lead to the use of IFRSs by U.S. issuers beginning in 2014. The SEC would make a decision in 2011 on whether adoption of IFRSs is in the public interest and would benefit investors. The proposed multiyear plan sets out several milestones that, if achieved, could lead to the use of IFRSs by U.S. issuers in their filings with the SEC. The top 20 companies in each industry, as determined by market capitalization, could elect to begin filing IFRSs financial statements for fiscal periods ending after December 15, 2009. If, in 2011, the SEC adopts IFRSs for all filers, the roadmap suggests mandatory filing for large accelerated filers beginning in 2014, accelerated filers in 2015, and nonaccelerated filers in 2016. The extended comment period ended in April 2009.

.236 The proposed roadmap sets forth seven milestones that will influence the SEC's decision to adopt IFRSs for all filers. These milestones relate to the following:

- Improvements in accounting standards
- Accountability and funding of the International Accounting Standards Committee Foundation (IASCF)
- Improvement in the ability to use interactive data for IFRSs reporting

- Education and training relating to IFRSs
- Limited early use of IFRSs when this would enhance comparability for U.S. investors
- Anticipated timing of future rulemaking by the SEC
- Implementation of the mandatory use of IFRSs by U.S. issuers

.237 Additionally, the roadmap discusses two alternatives for U.S. issuers that elect to use IFRSs to disclose U.S. GAAP information. Proposal A suggests that a U.S. issuer who elects to file IFRSs financial statements would provide the reconciling information from U.S. GAAP to IFRSs called for under IFRS 1, *First-time Adoption of International Financial Reporting Standards*, in a footnote to its audited financial statements. This information would include the restatement of and reconciliation from the prior year's financial statements and related disclosures. Proposal B suggests that U.S. issuers that elect to file IFRSs financial statements would provide the reconciling information from U.S. GAAP to IFRSs required under IFRS 1 and also would disclose on an annual basis certain unaudited supplemental U.S. GAAP financial information covering a three-year period. This unaudited supplemental financial information would be in the form of a reconciliation from IFRSs to U.S. GAAP.

.238 The roadmap does not address how the SEC would mandate IFRSs; however, the SEC noted that an option

> would be for the FASB to continue to be the designated standard setter for purposes of establishing the financial reporting standards in issuer filings with the Commission. In this option our presumption would be that the FASB would incorporate all provisions under IFRS, and all future changes to IFRS, directly into generally accepted accounting principles as used in the United States. This type of approach has been adopted by a significant number of other jurisdictions when they adopted IFRS as the basis of financial reporting in their capital markets.

.239 The full text of the roadmap can be viewed on the SEC Web site at http://sec.gov/rules/proposed/2008/33-8982.pdf.

.240 Since the issuance of the roadmap, new SEC Chairman Schapiro has indicated she favors a slowdown of the U.S. adoption of global accounting rules. Users are encouraged to closely monitor the progress of this initiative.

International Financial Reporting Standard for Small and Medium-sized Entities

.241 In July 2009, the IASB issued *International Financial Reporting Standard for Small and Medium-sized Entities* (IFRS for SMEs). *IFRS for SMEs* is an approximately 230 page, significantly reduced and simplified version of full IFRSs. In creating *IFRS for SMEs*, the IASB eliminated many accounting topics that are not generally relevant to private companies (for example, earnings per share and segment reporting), easing the financial reporting burden on private companies through a cost-benefit approach. *IFRS for SMEs* is a self-contained global accounting and financial reporting standard applicable to the general purpose financial statements of, and other financial reporting by, entities that are known in many countries as SMEs.

.242 *IFRS for SMEs* is intended to be used by entities that publish general purpose financial statements for external users and do not have public accountability. Under the IASB's definition, an entity has public accountability if it files or is in the process of filing its financial statements with a securities commission or other regulatory organization for the purpose of issuing any class of instruments in a public market, or if it holds assets in a fiduciary capacity for a broad group of outsiders. Examples of entities that hold assets in a fiduciary capacity include banks, insurance companies, brokers and dealers in securities, pension funds, and mutual funds. It is not the IASB's intention to exclude entities that hold assets in a fiduciary capacity for reasons incidental to their primary business (for example, travel agents, schools, and utilities) from utilizing *IFRS for SMEs*.

.243 Unlike public companies, U.S. private companies are not required to use a particular basis of accounting when preparing their financial statements. The factors that drive a private company's choice of which financial accounting and reporting framework to follow in preparing its financial statements depend upon each company's objectives and the needs of their financial statement users. Currently, private companies in the United States can prepare their financial statements in accordance with U.S. GAAP, as promulgated by FASB; an other comprehensive basis of accounting, such as cash or tax basis; or full IFRSs, among others. Now, with the issuance of *IFRS for SMEs*, U.S. private companies have an additional option.

.244 Some U.S. private companies may find the simplified *IFRS for SMEs* an attractive alternative to the more complicated and voluminous U.S. GAAP. Those private companies may find *IFRS for SMEs* to be a more relevant and less costly financial accounting and reporting standard than U.S. GAAP. Being based on full IFRS and missing many accounting topics, *IFRS for SMEs*, therefore, differs from U.S. GAAP in a variety of areas. Some of the key differences under *IFRS for SMEs* are the following:

- Disclosures are simplified in a number of areas including pensions, leases, and financial instruments.
- Last in, first out (LIFO) is prohibited.
- Goodwill and indefinite life intangible assets are amortized over a period not exceeding 10 years.
- Depreciation is based on a components approach.
- A simplified temporary difference approach to income tax accounting.
- Reversal of impairment charges, if certain criteria are met, is allowed.
- Accounting for financial assets and liabilities makes greater use of cost.

.245 Some key challenges that may be present in choosing to use *IFRS for SMEs* include understanding the differences between *IFRS for SMEs* and U.S. GAAP; the willingness of financial statement users to accept financial statements prepared under *IFRS for SMEs*; working with and accepting a more principles-based set of accounting standards compared to the more rules-based U.S. GAAP; the impact on taxes and tax planning strategies; and the impact on financial reporting metrics.

.246 The AICPA welcomes the introduction of *IFRS for SMEs* in the United States. Private companies should be allowed to choose the financial accounting and reporting framework that best suits their objectives and the needs of their financial statement users. *IFRS for SMEs* represents another valuable financial accounting and reporting option for private companies to consider using, depending upon their unique circumstances.

.247 In May 2008, the AICPA Governing Council voted to recognize the IASB as an accounting body for purposes of establishing international financial accounting and reporting principles. This amendment to appendix A of AICPA Rule 202, *Compliance With Standards* (AICPA, *Professional Standards*, vol. 2, ET sec. 202 par. .01), and Rule 203, *Accounting Principles* (AICPA, *Professional Standards*, vol. 2, ET sec. 203 par. .01), gives AICPA members the option to use IFRSs as an alternative to U.S. GAAP. As such, a key professional barrier to using IFRSs and, therefore, *IFRS for SMEs*, has been removed. CPAs may need to check with their state boards of accountancy to determine the status of reporting on financial statements prepared in accordance with *IFRS for SMEs* within their individual state. Any remaining barriers may come in the form of unwillingness by a private company's financial statement users to accept financial statements prepared under *IFRS for SMEs*, and a private company's expenditure of money, time, and effort to convert to *IFRS for SMEs*.

.248 Information about *IFRS for SMEs* and about the activities of the IASB can be found at www.ifrs.com. In addition, the AICPA and the IASCF jointly have developed a conference titled, "IFRS in North America 2009: The U.S. Perspective," to be held October 29–30 in New York. *IFRS for SMEs* will be addressed at the conference. For more information about the conference, visit www.cpa2biz.com.

AICPA Launches IFRS.com Web Site

.249 To assist in both awareness building and education, the AICPA launched the new Web site, www.ifrs.com, in May 2008. The site provides current information about developments in international convergence. Developed by the AICPA, in partnership with its marketing and technology subsidiary, CPA2Biz, www.ifrs.com provides a comprehensive set of resources for accounting professionals, auditors, financial managers, audit committees, and other users of financial statements.

.250 The Web site features tools and resources to help CPAs get acquainted with IFRSs, the surrounding issues, and available support. Resources include a history of convergence, a high level overview of the differences between IFRSs and U.S. GAAP, frequently asked questions, articles, textbooks, CPE courses and live conference training, helpful links, and assistance for audit committee members.

Recent Pronouncements

.251 AICPA auditing and attestation standards are applicable only to audits and attestation engagements of nonissuers. The Public Company Accounting Oversight Board (PCAOB) establishes auditing and attestation standards for audits of issuers. For information on pronouncements issued subsequent to the writing of this alert, please refer to the AICPA Web site at www.aicpa.org, the FASB Web site at www.fasb.org, and the PCAOB Web site at www.pcaob.org. You also may look for announcements of newly issued accounting standards in the *CPA Letter* and the *Journal of Accountancy*.

Recent Auditing and Attestation Pronouncements and Related Guidance

.252 The following table presents a list of recently issued audit and attestation pronouncements and related guidance.

Recent Auditing and Attestation Pronouncements and Related Guidance	
Statement on Auditing Standards (SAS) No. 116, *Interim Financial Information* (AICPA, *Professional Standards*, vol. 1, AU sec. 722) Issue Date: February 2009 (Applicable to audits conducted in accordance with generally accepted auditing standards [GAAS])	This standard amends AU section 722 to accommodate reviews of interim financial information of nonissuers, including companies offering securities pursuant to Securities and Exchange Commission (SEC) Rule 144A or participating in private equity exchanges. It is effective for reviews of interim financial information for interim periods beginning after December 15, 2009. Earlier application is permitted.
SAS No. 115, *Communicating Internal Control Related Matters Identified in an Audit* (AICPA, *Professional Standards*, vol. 1, AU sec. 325) Issue Date: October 2008 (Applicable to audits conducted in accordance with GAAS)	Replacing SAS No. 112, *Communicating Internal Control Related Matters Identified in an Audit* (AICPA, *Professional Standards*, vol. 1, AU sec. 325A), this standard defines the terms *deficiency in internal control*, *significant deficiency*, and *material weakness*; provides guidance on evaluating the severity of deficiencies in internal control identified in an audit of financial statements; and requires the auditor to communicate in writing, to management and those charged with governance, significant deficiencies and material weaknesses identified in an audit. It is effective for audits of financial statements for periods ending on or after December 15, 2009. Earlier implementation is permitted.
Statement on Standards for Attestation Engagements (SSAE) No. 15, *An Examination of an Entity's Internal Control Over Financial Reporting That Is Integrated With an Audit of Its Financial Statements* (AICPA, *Professional Standards*, vol. 1, AT sec. 501) Issue Date: October 2008	This statement establishes requirements and provides guidance that applies when a practitioner is engaged to perform an examination of the design and operating effectiveness of an entity's internal control over financial reporting (examination of internal control) that is integrated with an audit of financial statements (integrated audit). This SSAE is

Recent Auditing and Attestation Pronouncements and Related Guidance	
	effective for integrated audits for periods ending on or after December 15, 2008. Earlier implementation is permitted.
Interpretation No. 1, "Use of Electronic Confirmations," of AU section 330, *The Confirmation Process* (AICPA, *Professional Standards*, vol. 1, AU sec. 9330 par. .01–.08) Issue Date: April 2007 Revised Date: November 2008 (Interpretive publication)	This interpretation of AU section 330 addresses the use of electronic confirmations.
Interpretation No. 7, "Reporting on the Design of Internal Control," of AT section 101, *Attest Engagements* (AICPA, *Professional Standards*, vol. 1, AT sec. 9101 par. .59–.69) Issue Date: December 2008 (Interpretive publication)	This interpretation of AT section 101 addresses how a practitioner may report on the suitability of the design of an entity's internal control over financial reporting for preventing or detecting and correcting material misstatements of the entity's financial statements on a timely basis.
Technical Questions and Answers (TIS) section 8700.01, "Effect of FASB ASC 855 on Accounting Guidance in AU Section 560" (AICPA, *Technical Practice Aids*) Issue Date: September 2009 (Nonauthoritative)	This question and answer addresses whether the accounting guidance in AU section 560, *Subsequent Events* (AICPA, *Professional Standards*, vol. 1) is effected by the issuance of Financial Accounting Standards Board (FASB) *Accounting Standards Codification* (ASC) 855, *Subsequent Events*.
TIS section 8700.02, "Auditor Responsibilities for Subsequent Events" (AICPA, *Technical Practice Aids*) Issue Date: September 2009 (Nonauthoritative)	This question and answer discusses whether the auditor's responsibilities under AU section 560 are changed as a result of the issuance of FASB ASC 855.
TIS section 1500.07, "Disclosure Concerning Subsequent Events in OCBOA Financial Statements" (AICPA, *Technical Practice Aids*) Issue Date: July 2009 (Nonauthoritative)	This question and answer addresses whether full disclosure financial statements prepared on an other comprehensive basis of accounting should contain the disclosures set forth in Financial Accounting Standards Board (FASB) *Accounting Standards Codification* (ASC) 855, *Subsequent Events*.

(continued)

Recent Auditing and Attestation Pronouncements and Related Guidance	
TIS section 1900.01, "Condensed Interim Financial Reporting by Nonissuers" (AICPA, *Technical Practice Aids*) Issue Date: January 2009 (Nonauthoritative)	This question and answer indicates that when preparing condensed interim financial statements, nonissuers may analogize to the guidance in Article 10 of SEC Regulation S-X regarding form and content because Accounting Principles Board (APB) Opinion No. 28, *Interim Financial Reporting*, does not provide a reporting framework. APB Opinion No. 28 is codified primarily at FASB ASC 270, *Interim Reporting*.
TIS section 9150.25, "Determining Whether Financial Statements Have Been Prepared by the Accountant" (AICPA, *Technical Practice Aids*) Issue Date: December 2008 (Nonauthoritative)	This question and answer discusses what an accountant should consider in determining whether he or she has prepared the financial statements of a nonissuer.
TIS section 1100.15, "Liquidity Restrictions" (AICPA, *Technical Practice Aids*) Issue Date: October 2008 (Nonauthoritative)	This question and answer discusses auditing and accounting issues related to withdrawal restrictions placed on short-term investments by a money market fund or its trustee.
Public Company Accounting Oversight Board (PCAOB) Auditing Standard No. 6, *Evaluating Consistency of Financial Statements* (AICPA, *PCAOB Standards and Related Rules*, Rules of the Board, "Standards") Issue Date: September 2008 (Applicable to audits conducted in accordance with PCAOB standards)	This standard and its related amendments update the auditor's responsibilities to evaluate and report on the consistency of a company's financial statements and align the auditor's responsibilities with FASB Statement No. 154, *Accounting Changes and Error Corrections—a replacement of APB Opinion No. 20 and FASB Statement No. 3*, which is codified at FASB ASC 250, *Accounting Changes and Error Corrections*. This standard also improves the auditor reporting requirements by clarifying that the auditor's report should indicate whether an adjustment to previously issued financial statements results from a change in accounting principles or the correction of a misstatement. It is effective November 15, 2008.

Recent Auditing and Attestation Pronouncements and Related Guidance	
PCAOB Rule 3526, *Communication with Audit Committees Concerning Independence* (AICPA, *PCAOB Standards and Related Rules*, Rules of the Board, "Rules") Issue Date: August 2008 (Applicable to audits conducted in accordance with PCAOB standards)	Rule 3526 requires the registered public accounting firm to • describe in writing, to the audit committee of the issuer, all relationships between the registered public accounting firm or any affiliates of the firm and the potential audit client or persons in financial reporting oversight roles at the potential audit client that, as of the date of the communication, may reasonably be thought to bear on independence. • discuss with the audit committee of the issuer the potential effects of any relationships that could affect independence, should they be appointed as the issuer's auditor. • document the substance of these discussions. These discussions should occur at least annually. The board also adjusted the implementation schedule for Rule 3523, *Tax Services for Persons in Financial Reporting Oversight Roles* (AICPA, *PCAOB Standards and Related Rules*, Rules of the Board, "Rules"), as it applies to tax services. The board agreed not to apply Rule 3523 to tax services provided on or before December 31, 2008, when those services are provided during the audit period and are completed before the professional engagement period begins. The amendments to Rule 3523 became effective August 28, 2008. The remaining provisions of Rule 3526 became effective on September 30, 2008.
PCAOB Conforming Amendments to the Interim Auditing Standards (AICPA, *PCAOB Standards and Related Rules*, Rules of the Board, "Standards")	In conjunction with the PCAOB's adoption of Auditing Standard No. 6, the PCAOB also adopted a number of conforming amendments to its interim standards. The conforming

(continued)

Recent Auditing and Attestation Pronouncements and Related Guidance	
Issue Date: November 15, 2008 (Applicable to audits conducted in accordance with PCAOB standards)	amendments can be found in appendix 2 of PCAOB Release No. 2008-001 at www.pcaob.org/Rules/Docket_023/PCAOB_Release_No._2008-001_–_Evaluating_Consistency.pdf.
PCAOB Staff Audit Practice Alert No. 4, *Auditor Considerations Regarding Fair Value Measurements, Disclosures, and Other-Than-Temporary Impairments* (AICPA, *PCAOB Standards and Related Rules*, PCAOB Staff Guidance, sec. 400.04) Issue Date: April 2009 (Applicable to audits conducted in accordance with PCAOB standards)	This staff audit practice alert is designed to inform auditors about potential implications of the FASB Staff Positions on reviews of interim financial information and annual audits. This alert addresses the following topics: • Reviews of interim financial information • Audits of financial statements, including integrated audits • Disclosures • Auditor reporting considerations.
PCAOB Staff Audit Practice Alert No. 3, *Audit Considerations in the Current Economic Environment* (AICPA, *PCAOB Standards and Related Rules*, PCAOB Staff Guidance, sec. 400.03) Issue Date: December 2008 (Applicable to audits conducted in accordance with PCAOB standards)	This practice alert is designed to assist auditors in identifying matters related to the current economic environment that might affect audit risk and require additional emphasis. The practice alert addresses the following six main areas: overall audit considerations, auditing fair value measurements, auditing accounting estimates, auditing the adequacy of disclosures, auditor's consideration of a company's ability to continue as a going concern, and additional audit considerations for selected financial reporting areas.

Recent Accounting Pronouncements and Related Guidance

.253 The following table presents a list of recently issued accounting pronouncements and related guidance.

Recent Accounting Pronouncements and Related Guidance	
Financial Accounting Standards Board (FASB) *Accounting Standards Codification*™ (ASC) Accounting Standard Update (ASU) No. 2009-06 (September 2009)	*Income Taxes (Topic 740)—Implementation Guidance on Accounting for Uncertainty in Income Taxes and Disclosure Amendments for Nonpublic Entities*
FASB ASC ASU No. 2009-05 (August 2009)	*Fair Value Measurements and Disclosures (Topic 820)—Measuring Liabilities at Fair Value*
FASB ASC ASU No. 2009-04 (August 2009)	*Accounting for Redeemable Equity Instruments—Amendment to Section 480-10-S99*
FASB ASC ASU No. 2009-03 (August 2009)	*SEC Update—Amendments to Various Topics Containing SEC Staff Accounting Bulletins*
FASB ASC ASU No. 2009-02 (June 2009)	*Omnibus Update—Amendments to Various Topics for Technical Corrections*
FASB ASC ASU No. 2009-01 (June 2009)	*Topic 105—Generally Accepted Accounting Principles—amendments based on—Statement of Financial Accounting Standards No. 168—The FASB Accounting Standards Codification*™ and the Hierarchy of Generally Accepted Accounting Principles
FASB Statement No. 168 (June 2009) (Codified at FASB ASC 105, *Generally Accepted Accounting Principles*)	*The* FASB Accounting Standards Codification™ *and the Hierarchy of Generally Accepted Accounting Principles—a replacement of FASB Statement No. 162*
FASB Statement No. 167[6] (June 2008)	*Amendments to FASB Interpretation No. 46(R) —an amendment of FASB Statement No. 140*
FASB Statement No. 166[7] (June 2009)	*Accounting for Transfers of Financial Assets—an amendment of FASB Statement No. 140*

(continued)

[6] See footnote 3.

[7] See footnote 3.

Recent Accounting Pronouncements and Related Guidance	
FASB Statement No. 165 (May 2009) (Codified at FASB ASC 855, *Subsequent Events*)	*Subsequent Events*
FASB Statement No. 164[8] (May 2009)	*Not-for-Profit Entities: Mergers and Acquisitions—Including an amendment of FASB Statement No. 142*
Governmental Accounting Standards Board (GASB) Statement No. 56 (March 2009)	*Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards*
GASB Statement No. 55 (March 2009)	*The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*
GASB Statement No. 54 (February 2009)	*Fund Balance Reporting and Governmental Fund Type Definitions*
GASB Statement No. 53 (December 2007)	*Accounting and Financial Reporting for Derivative Instruments*
GASB Concepts Statement No. 5 (November 2008)	*Service Efforts and Accomplishments Reporting—an amendment of GASB Concepts Statement No. 2*
GASB Technical Bulletin 2008-1 (December 2008)	*Determining the Annual Required Contribution Adjustment for Postemployment Benefits*
FASB Emerging Issues Task Force (EITF) Issues (Various dates)	Go to www.fasb.org/eitf/agenda.shtml for a complete list of EITF Issues.
FASB Staff Positions (FSPs) (Various dates)	Go to www.fasb.org for a complete list of FSPs.
Technical Questions and Answers (TIS) section 6910.30, "Disclosure Requirements of Investments for Nonregistered Investment Partnerships When Their Interest in an Investee Fund Constitutes Less Than 5 Percent of the Nonregistered Investment Partnership's Net Assets" (AICPA, *Technical Practice Aids*) Issue Date: August 2009 (Nonauthoritative)	This question and answer discusses the disclosure requirements for investments for nonregistered investment partnerships.

[8] See footnote 3.

Recent Accounting Pronouncements and Related Guidance	
TIS section 6910.31, "The Nonregistered Investment Partnership's Method for Calculating Its Proportional Share of Any Investments Owned by an Investee Fund in Applying the '5 Percent Test' Described in TIS Section 6910.30" (AICPA, *Technical Practice Aids*) Issue Date: August 2009 (Nonauthoritative)	This question and answer discusses the method of determining the application of TIS section 6910.30 to nonregistered investment partnerships.
TIS section 6910.32, "Additional Financial Statement Disclosures for Nonregistered Investment Partnerships When the Partnership Has Provided Guarantees Related to the Investee Fund's Debt" (AICPA, *Technical Practice Aids*) Issue Date: August 2009 (Nonauthoritative)	This question and answer discusses additional disclosures required for nonregistered investment partnerships.
TIS section 1600.04, "Presentation of Assets at Current Values and Liabilities at Current Amounts in Personal Financial Statements" (AICPA, *Technical Practice Aids*) Issue Date: June 2009 (Nonauthoritative)	This question and answer discusses the definitions of *current values* and *current amounts* for personal financial statements.
TIS section 6931.11, "Fair Value Measurement Disclosures for Master Trusts" (AICPA, *Technical Practice Aids*) Issue Date: March 2009 (Nonauthoritative)	This question and answer indicates that the disclosures required by paragraphs 32–34 of FASB Statement No. 157, *Fair Value Measurements*, are required for individual investments under a master trust arrangement and are not required for the plan's total interest in the master trust.
TIS section 6995.02, "Evaluation of Capital Investments in Corporate Credit Unions for Other-Than-Temporary Impairment" (AICPA, *Technical Practice Aids*) Issue Date: February 2009 (Nonauthoritative)	This question and answer highlights the authoritative literature that helps a corporate credit union evaluate its membership capital shares and paid-in capital in the U.S. Central Federal Credit Union for other-than-temporary impairment charges at December 31, 2008.

(continued)

Recent Accounting Pronouncements and Related Guidance	
TIS section 6995.01, "Financial Reporting Issues Related to Actions Taken by the National Credit Union Administration on January 28, 2009 in Connection With the Corporate Credit Union System and the National Credit Union Share Insurance Fund" (AICPA, *Technical Practice Aids*) Issue Date: January 2009 (Nonauthoritative)	This question and answer presents alternative views regarding whether the actions of the National Credit Union Administration constitute a type 1 or type 2 subsequent event with regard to the valuation of a federally insured credit union's National Credit Union Share Insurance Fund deposit at December 31, 2008. Additionally, this question and answer presents alternative views on when and how the obligation for the insurance premium should be recognized for financial reporting purposes.
TIS section 6910.29, "Allocation of Unrealized Gain (Loss), Recognition of Carried Interest, and Clawback Obligations" (AICPA, *Technical Practice Aids*) Issue Date: January 2009 (Nonauthoritative)	This question and answer discusses how cumulative unrealized gains (losses), carried interest, and clawback should be reflected in the equity balances of each class of shareholder or partner at the balance sheet date when preparing financial statements of an investment partnership, in accordance with U.S. generally accepted accounting principles, in which capital is reported by investor class. In particular, this question and answer asks if cumulative period-end unrealized gains and losses should be allocated as if realized in accordance with the partnership's governing documents prior to the date, time, or event specified in the partnership agreement.
TIS section 1900.01, "Condensed Interim Financial Reporting by Nonissuers" (AICPA, *Technical Practice Aids*) Issue Date: January 2009 (Nonauthoritative)	This question and answer indicates that when preparing condensed interim financial statements, nonissuers may analogize to the guidance in Article 10 of SEC Regulation S-X regarding form and content because Accounting Principles Board (APB) Opinion No. 28, *Interim Financial Reporting*, does not provide a reporting framework. APB Opinion No. 28 is codified primarily at FASB ASC 270, *Interim Reporting*.
TIS section 6300.36, "Prospective Unlocking" (AICPA, *Technical Practice Aids*) Issue Date: December 2008 (Nonauthoritative)	This question and answer discusses when an insurance company may change its original policyholder benefit liability assumptions.

Recent Accounting Pronouncements and Related Guidance	
TIS section 1100.15, "Liquidity Restrictions" (AICPA, *Technical Practice Aids*) Issue Date: October 2008 (Nonauthoritative)	This question and answer discusses auditing and accounting issues related to withdrawal restrictions placed on short-term investments by a money market fund or its trustee.

Recent AICPA Independence and Ethics Pronouncements

.254 Audit Risk Alert *Independence and Ethics Developments—2009* (product no. 0224709) contains a complete update on new independence and ethics pronouncements. This alert will heighten your awareness of independence and ethics matters likely to affect your practice. Obtain this alert by calling the AICPA at (888) 777-7077 or visiting www.cpa2biz.com.

On the Horizon

.255 Auditors should keep abreast of auditing and accounting developments and upcoming guidance that may affect their engagements. The following sections present brief information about some ongoing projects that have particular significance to the health care industry or that may result in significant changes. Remember that exposure drafts are nonauthoritative and cannot be used as a basis for changing existing standards.

.256 The following table lists the various standard setting bodies' Web sites, through which information may be obtained on outstanding exposure drafts, including downloading exposure drafts. These Web sites contain in-depth information about proposed standards and other projects in the pipeline. Many more accounting and auditing projects exist in addition to those discussed here. Readers should refer to information provided by the various standard setting bodies for further information.

Standard Setting Body	*Web Site*
AICPA Auditing Standards Board	www.aicpa.org/Professional+Resources/Accounting+and+Auditing/Audit+and+Attest+Standards/Auditing+Standards+Board/
Financial Accounting Standards Board	www.fasb.org
Governmental Accounting Standards Board	www.gasb.org
Professional Ethics Executive Committee	www.aicpa.org/Professional+Resources/Professional+Ethics+Code+of+Professional+Conduct/Professional+Ethics/
Public Company Accounting Oversight Board	www.pcaob.org
Securities and Exchange Commission	www.sec.gov

Overhaul Project—AICPA Audit and Accounting Guide *Health Care Entities*

.257 The AICPA is continuing to make progress overhauling the AICPA Audit and Accounting Guide *Health Care Entities*, addressing numerous accounting, auditing, industry, and regulatory issues that have transpired since this guide was originally issued in 1996. During this project, the AICPA will continue to issue annual editions of the guide, updated to reflect recent audit and accounting pronouncements.

Auditing and Attestation Pipeline—Nonissuers

ASB Clarity Project

.258 In response to growing concerns about the complexity of standards, the ASB has commenced a large-scale clarity project to revise all existing auditing standards so they are easier to read and understand. Over the next two or three years, the ASB will be redrafting all of the existing auditing sections contained in the *Codification of Statements on Auditing Standards* (AU sections of the AICPA's *Professional Standards*) to apply the clarity drafting conventions and converge with the International Standards on Auditing (ISAs) issued by the International Auditing and Assurance Standards Board (IAASB). The ASB proposes that, except to address current issues, all redrafted standards will become effective at the same time. Only those standards needing to address current issues would have earlier effective dates. The ASB believes that a single effective date will ease the transition to, and implementation of, the redrafted standards. The effective date will be long enough after all redrafted statements are finalized to allow sufficient time for training and updating of firm audit methodologies. Currently, the date is expected to be for audits of financial statements for periods beginning no earlier than December 15, 2010. This date depends on satisfactory progress being made and will be amended, should that prove necessary. See the explanatory memorandum, "Clarification and Convergence," and the discussion paper, *Improving the Clarity of ASB Standards* at www.aicpa.org/Professional+Resources/Accounting+and+Auditing/Audit+and+Attest+Standards/Improving+the+Clarity+of+ASB+Standards.htm.

Compliance Auditing

.259 In January 2009, the ASB issued a proposed SAS, *Compliance Auditing.*[9] The proposed SAS would supersede SAS No. 74, *Compliance Auditing Considerations in Audits of Governmental Entities and Recipients of Governmental Financial Assistance* (AICPA, Professional Standards, vol. 1, AU sec. 801). The proposed SAS was issued as the direct result of the AICPA's Compliance Auditing Task Force, which was formed as a result of the President's Council on Integrity and Efficiency (PCIE) report, Report on National Single Audit Sampling Project.

.260 The proposed SAS clarifies its applicability to, and provides more detailed guidance for, compliance audits. As a result, it is expected that the application of the proposed SAS may change the way an auditor performs a

[9] The proposed Statement on Auditing Standards (SAS) *Compliance Audits* was approved at the August 2009 Auditing Standards Board meeting. Visit the AICPA Web site to see the newly released SAS.

compliance audit. However, how significantly the proposed SAS will affect a firm's compliance audits will depend on how closely the firm has been following the audit guidance in this guide and adapting existing AICPA SASs to compliance audits.

.261 A summary of the potential effects of the proposed SAS on compliance audits are as follows:

- The proposed SAS, which was prepared using the ASB's new clarity format, presents a more detailed description of auditor requirements than SAS No. 74, which should result in a better understanding of the compliance audit requirements. It also includes key definitions, the overall objectives of the standards, and application guidance and explanatory materials.
- The applicability section of the standard includes compliance audits beyond those performed under OMB Circular A-133 *Audits of States, Local Governments, and Non-Profits*, such as audits performed under certain federal agency audit guides (for example, audits conducted in accordance with the U.S. Department of Housing and Urban Development *Consolidated Audit Guide*).
- The proposed SAS includes in its requirements certain compliance auditing considerations that previously had been discussed only in the Government Auditing Standards *and Circular A-133 Audits* Audit Guide. The inclusion of this material in the standard will result in the guidance being applied to all compliance audits covered by the proposed SAS, instead of only Circular A-133 audits.
- The proposed SAS clarifies the applicability of other AU sections to compliance audits, which may result in practice changes depending on how a firm previously interpreted the applicability of other auditing standards to a compliance audit.

.262 The proposed SAS would apply when an auditor is engaged to perform a compliance audit in accordance with all of the following:

- Generally accepted auditing standards
- The standards for financial audits under *Government Auditing Standards*
- A governmental audit requirement (defined as a governmental requirement established by law, regulation, rule, or provision of contracts or grant agreements requiring that an entity undergo an audit of its compliance with applicable compliance requirements related to one or more government programs that the entity administers)

.263 As mentioned previously, the proposed SAS encompasses compliance audits beyond those performed under Circular A-133; therefore, more compliance audits will be subject to the requirements of the proposed SAS. The proposed SAS does not apply to the financial statement audit component related to a compliance audit.

.264 Readers may obtain a copy of the proposed SAS and track its current status through the Audit and Attest section of the AICPA's Web site at www.aicpa.org/Professional+Resources/Accounting+and+Auditing/Audit+and+Attest+Standards/.

Exposure Draft to Revise Standards for Compilation and Review Engagements

.265 The Accounting and Review Services Committee (ARSC) issued an exposure draft that would revise the standards for compilation and review engagements. The changes would affect the interplay between the standards and independence rules, permitting an accountant to issue a review report on financial statements when the accountant's independence is impaired by performing certain nonattest services (described in the exposure draft as internal control services) that were designed to improve the reliability of the client's financial information.

.266 The exposure draft includes a trio of proposed standards: Framework and Objectives for Performing and Reporting on Compilation and Review Engagements, Compilation of Financial Statements, and Review of Financial Statements. In drafting the proposed standards, the ARSC considered recommendations from the Private Company Practice Section (PCPS) Reliability Task Force. The ARSC and PCPS believe the proposed standards will respond to many concerns of smaller business owners, users of small business financial statements, and CPAs who serve smaller entities.

.267 The PCPS task force recommended that the ARSC consider revising its standards for situations in which an accountant's independence is impaired in connection with the performance of a nonattest service relating to the design or operation of an aspect of internal control over financial reporting. These nonattest services help management prepare higher quality or more reliable financial statements.

.268 The proposed standards also would harmonize the AICPA's review standard with the IAASB's review standard, International Standard on Review Engagements No. 2400, *Engagements to Review Financial Statements*.

.269 Significant proposed changes to the Statements on Standards for Accounting and Review Services include the following:

- The introduction of new terms such as *moderate assurance*, *review evidence*, and *review risk* to the review literature to harmonize with international review standards.
- A discussion of materiality in the context of a review engagement.
- A requirement that an accountant establish an understanding with management regarding the services to be performed through a written communication (that is, an engagement letter).
- The establishment of enhanced documentation requirements for compilation and review engagements.
- Guidance for practitioners who are engaged to perform a compilation or review engagement when they also have been engaged to perform nonattest services. The guidance includes reporting requirements for instances in which the accountant's independence is impaired due to the performance of these services.
- The ability for an accountant to include a general description in the accountant's compilation report regarding the reason(s) for an independence impairment.

.270 The comment deadline is July 31, 2009. The proposed effective date is for compilations and reviews of financial statements for periods beginning on or after December 15, 2010. Early application would be permitted. For further information on this project, visit www.aicpa.org/Professional+Resources/Accounting+and+Auditing/Audit+and+Attest+Standards/ARSC+Reliability+Project.htm.

Implementation Guidance for Compilation and Review Standards

.271 The AICPA is working on several products to further your knowledge of the new compilation and review standards. The first product is our annual alert *Compilation and Review Engagements—2009*. This alert provides an annual update on issues affecting compilation and review engagements and will focus on the proposed new standards, among other issues, affecting practitioners performing compilation and review engagements. This alert is scheduled to be released in December 2009, just in time for your 2009 compilation and review engagement planning. The second product is a new alert, *Understanding the Revised Standards for Performing Compilation and Review Engagements*. This alert will be released shortly after the new standards are finalized in early 2010 and will focus on information for entities expecting to early adopt the new standards. The last product is a brand new AICPA guide, *Compilation and Review Engagements*, which will provide additional information on implementing the new compilation and review standards and understanding internal control services. It also will include illustrative letters, sample reports, and case studies. This guide is expected to be available in spring 2010. See www.cpa2biz.com for further information.

Auditing and Attestation Pipeline—Issuers

PCAOB Risk Assessment Standards

.272 In October 2008, the PCAOB proposed seven new auditing standards to update and supersede the current risk assessment standards. The PCAOB chairman noted that the proposals demonstrate the view that the risk of fraud is a central part of the audit process and not a separate consideration. The proposed standards integrate the risk assessment standards with the standard for the audit of internal control over financial reporting. Many of the IAASB's risk assessment standards were utilized in creating these proposed standards, and efforts were made to reduce any unnecessary differences. Each of these proposed standards has a statement of objective for the auditor, which was loosely adapted from the ISAs. This is an example of the move in the United States from rules-based to principles-based accounting and auditing standards because these objectives do not state required outcomes. The seven proposed standards are as follows:

- Audit Risk in an Audit of Financial Statements
- Audit Planning and Supervision
- Identifying and Assessing Risks of Material Misstatement
- The Auditor's Responses to the Risks of Material Misstatement
- Evaluating Audit Results
- Consideration of Materiality in Planning and Performing an Audit
- Audit Evidence

.273 In February 2009, the Center for Audit Quality (CAQ) issued a comment letter on the proposed standards. Readers can review the full text of the comment letter at http://thecaq.org/newsroom/pdfs/CAQCommentLetter-PCAOBRiskAssessmentAuditStds.pdf. The comment period for these proposed standards ended in February 2009. As with any new auditing standard or amendment to a PCAOB standard, after adoption by the PCAOB, the standards will be submitted to the SEC for approval.

Engagement Quality Review

.274 In March 2009, the PCAOB reproposed an auditing standard on engagement quality review for public comment. The PCAOB made substantial changes to the proposed auditing standard because it was first proposed in February 2008. The proposal would supersede the PCAOB's current audit quality control standard and would apply to all audit engagements and engagements to review interim financial information conducted pursuant to the standards of the PCAOB. The proposed standard provides a framework for an engagement quality reviewer to objectively evaluate the significant judgments made by the engagement team and the conclusions reached in forming an overall conclusion about the engagement. In July 2009, the PCAOB voted to adopt this standard as Auditing Standard No. 7, *Engagement Quality Review*. This standard will be effective, subject to SEC approval, for both engagement quality reviews of audits and interim reviews for fiscal years beginning on or after December 15, 2009.

Concept Release on Audit Confirmations

.275 In April 2009, the PCAOB issued a concept release for public comment on possible revisions to AU section 330, *The Confirmation Process* (AICPA, *Professional Standards,* vol. 1). Confirmations are typically an important source of evidence for auditors because independent third party sources verify the data on the confirmation. The PCAOB's concept release addresses the following nine areas of possible change to the current confirmation guidance:

- Expands the definition of confirmation to include direct access to information held by a third party
- Establishes a presumption that the auditor will request the confirmation of accounts receivable
- Discusses factors to consider in designing confirmation requests
- Updates the requirement for maintaining control over confirmation requests for the advances in technology
- Provides further direction on evaluating the reliability of confirmation responses
- Eliminates the ability for the auditor to omit performing alternative procedures for nonresponses to positive confirmation requests
- Considerations for when management requests an auditor to not confirm a select account, transaction, and so on
- Conducts an evaluation of disclaimers and restrictive language on confirmation responses
- Considers whether the use of negative confirmations should continue to be allowed

.276 Generally speaking, the concept release does not contemplate major changes to the confirmation process; rather, it addresses developments in technology and related risk factors. Comments were due back to the PCAOB by the end of May 2009. Readers should be alert to developments on this issue.

Accounting Pipeline

FASB and IASB Memorandum of Understanding

.277 In September 2008, FASB and the IASB updated their "Memorandum of Understanding" (MoU), originally published in 2006, to reaffirm their respective commitments to the development of high quality, compatible accounting standards that could be used for both domestic and cross-border financial reporting. In developing the original MoU, FASB and the IASB agreed on priorities and established milestones as part of a joint work program to develop new common standards that improve the financial information reported to investors. FASB and the IASB agreed that the goal of joint projects is to produce common, principles-based standards, subject to the required due process. In the MoU, the boards identified the following 11 convergence topics on which to focus:

- Business combinations
- Financial instruments
- Financial statement presentation
- Intangible assets
- Leases
- Liabilities and equity distinctions
- Revenue recognition
- Consolidations
- Derecognition
- Fair value measurement
- Postemployment benefits (including pensions)

.278 Both FASB and the IASB note that their individual and joint efforts are not limited to the preceding items, but they remain committed to the MoU. FASB and the IASB also have several other joint projects in process, including the conceptual framework project, emissions trading schemes, insurance contracts, and income taxes.

.279 Readers also are encouraged to monitor developments on the AICPA's Web site, www.ifrs.com, in addition to the FASB, IASB, and SEC Web sites. The growing acceptance of IFRSs as a basis for U.S. financial reporting could represent a fundamental change for the U.S. accounting profession.

Other Accounting Projects

.280 Additionally, FASB has the following projects underway:

- Going concern
- Credit crisis projects that include the following:
    - Measuring liabilities under FASB ASC 820
    - Embedded credit derivatives scope exceptions
    - Recoveries of other-than-temporary impairments

- — Improving disclosures about fair value measurements
- — Applying fair value to interests in alternative investments

- Phase 2 of the applicability of FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes—an interpretation of FASB Statement No. 109*, for private entities (FASB Interpretation No. 48 is codified at FASB ASC 740, *Income Taxes*)
- Disclosure of certain loss contingencies
- Loan loss disclosures
- Disclosure framework
- Phase 2 of postretirement benefit obligations, including pensions
- Oil and gas disclosures
- Treatment of base jackpot liabilities of casinos

.281 FASB and the IASB established an advisory group, the Financial Crisis Advisory Group (FCAG), which is comprised of senior leaders with international experience in financial markets. The FCAG will advise FASB and the IASB about the standard setting implications of the global financial crisis, as well as changes to the global regulatory environment. Readers should refer to http://fasb.org/fcag/index.shtml for additional information.

Current GASB Projects

.282 GASB currently has a variety of projects in process. Some of these projects are as follows:

- Chapter 9 of the United States Bankruptcy Code project, which will provide accounting and financial reporting guidance for governments that have been granted protection from creditors under Chapter 9 of the United States Bankruptcy Code. The project includes an analysis of the financial reporting consequences for governments that have been granted protection under Chapter 9. "Protection" may include modifications to the terms and conditions of certain of the government's debt issuances and relief from burdensome provisions of certain executory contracts and unexpired lease commitments.
- Codification of Pre-November 30, 1989, FASB Pronouncements, to specifically identify provisions in FASB Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the AICPA Committee on Accounting Procedure, issued on or before November 30, 1989 (collectively, the FASB pronouncements) as referenced in paragraph 17 of GASB Statement No. 34, that do not conflict with or contradict GASB pronouncements.
- Conceptual Framework—Recognition and Measurement Attributes, which has two primary objectives:
  - — The first objective is to develop recognition criteria for whether information should be reported in state and local governmental financial statements and when that information should be reported.

- — The second objective is to consider the measurement attribute or measurement attributes (for example, historical cost or fair value) that, conceptually, should be used in governmental financial statements. This project ultimately will lead to a Concepts Statement.

- Postemployment Benefit Accounting and Financial Reporting, to consider the possibility of improvements to the existing standards of accounting and financial reporting for postemployment benefits—including pension benefits and OPEB—by state and local governmental employers and by the trustees, administrators, or sponsors of pension or OPEB plans. One objective of this project is to improve accountability, or the transparency of financial reporting, in regard to the financial effects of employers' commitments and actions related to pension benefits and OPEB. This objective would include improving the information provided to help financial report users assess the degree to which interperiod equity has been achieved. The other objective of this project is to improve the usefulness of information for decisions or judgments of relevance to the various users of the general purpose external financial reports of governmental employers and pension or OPEB plans. This project currently has an outstanding Invitation to Comment at www.gasb.org.
- Certain Implementation Issues Related to OPEB, to consider whether to modify certain requirements related to the measurement of actuarial liabilities for OPEB by agent employers. The issues relate primarily to the interface between the accounting and financial reporting requirements of GASB Statement Nos. 43 and 45 in regard to agent multiple-employer OPEB plans and specifically include consideration of (1) the timing and frequency of the measurement of actuarial liabilities for OPEB by agent employers and (2) the guidelines regarding use of the alternative measurement method by agent employers with small individual OPEB plans.
- Financial Instruments Omnibus, to consider potential revisions to existing standards regarding financial reporting and disclosure requirements that could address significant issues that have been identified in practice since the issuance of GASB Statement No. 31. This project includes five project elements—external investment pools, custodial credit risk of deposits that participate in deposit placement services, unallocated insurance contracts, interest rate risk disclosures for mutual funds, and reporting realized gains and losses. In addition, the existing portions of GASB Statement No. 53 relating to swap terminations, revenue-based contract exclusions, and investor's initial rate of return will be addressed.

.283 Readers should be alert for the issuance of due process documents. More information about these and other GASB projects can be found at www.gasb.org/project_pages/index.html.

Resource Central

.284 The following are various resources that practitioners engaged in the health care industry may find beneficial.

Publications

.285 Practitioners may find the following publications useful. Choose the format best for you—online, print, or CD-ROM.

- Audit and Accounting Guide *Health Care Entities* (2009) (product no. 012619 [paperback], WHC-XX [online with the associated Audit Risk Alert], or DHC-XX [CD-ROM])
- Audit and Accounting Guide *Not-for-Profit Entities* (2009) (product no. 012649 [paperback], WNP-XX [online with the associated Audit Risk Alert], or DNP-XX [CD-ROM])
- Audit and Accounting Guide Government Auditing Standards *and Circular A-133 Audits* (2008) (product no. 012748 [paperback], WRF-XX [online with the associated Audit Risk Alert], or DRF-XX [CD-ROM])
- Audit and Accounting Guide *State and Local Governments* (2009) (product no. 012669 [paperback], WGG-XX [online with the associated Audit Risk Alert], or DGG-XX [CD-ROM])
- Audit Guide *Analytical Procedures* (2008) (product no. 012558 [paperback], WAN-XX [online], or DAN-XX [CD-ROM])
- Audit Guide *Assessing and Responding to Audit Risk in a Financial Statement Audit* (2006) (product no. 012456 [paperback] or WRA-XX [online])
- Audit Guide *Auditing Revenue in Certain Industries* (2009) (product no. 012519 [paperback], WAR-XX [online], or DAR-XX [CD-ROM])
- Audit Guide *Audit Sampling* (2008) (product no. 012538 [paperback], WAS-XX [online], or DAS-XX [CD-ROM])
- Audit Guide *Service Organizations: Applying SAS No. 70, as Amended* (2009) (product no. 012779 [paperback], WSV-XX [online], or DSV-XX [CD-ROM])
- Audit Risk Alert *State and Local Governmental Developments—2009* (product no. 0224309 [paperback] or WGG-XX [online with the associated Audit and Accounting Guide])
- Audit Risk Alert *Not-for-Profit Entities Industry Developments—2009* (product no. 0224209 [paperback] or WNP-XX [online with the associated Audit and Accounting Guide])
- Audit Risk Alert Government Audit Standards *and Circular A-133 Audits—2008* (product no. 022458 [paperback] or WRF-XX [online with the associated Audit and Accounting Guide])
- Audit Risk Alert *Communicating Internal Control Related Matters in an Audit—Understanding SAS No. 115* (product no. 022539 [paperback], WIA-XX [online], or DIA-XX [CD-ROM])
- Audit Risk Alert *Compilation and Review Developments—2008* (product no. 022309 [paperback], WCR-XX [online], or DCR-XX [CD-ROM])
- Audit Risk Alert *Current Economic Crisis: Accounting and Auditing Considerations—2009* (product no. 0223308 [paperback], WGE-XX [online], or DGE-XX [CD-ROM])

- Audit Risk Alert *Independence and Ethics Developments—2009* (product no. 0224709 [paperback], WIA-XX [online], or DIA-XX [CD-ROM])
- Checklists and Illustrative Financial Statements *Health Care Organizations* (product no. 009029 [paperback] or WHE-CL [online])
- *Guide to Fraud in Governmental and Not-for-Profit Environments, Revised Edition* (product no. 091032 [paperback])
- *Accounting Trends & Techniques, 62nd Edition* (product no. 009900 [paperback] or WAT-XX [online])
- *Audit and Accounting Manual* (2009) (product no. 0051309 [paperback], WAM-XX [online], or AAM-XX [loose leaf])
- Audit and Accounting Practice Aid *Independence Compliance: Checklists and Tools for Complying With AICPA and GAO Independence Requirements* (product no. 006661 [paperback])
- Audit and Accounting Practice Aid *Independence Compliance: Checklists and Tools for Complying With AICPA, SEC, and PCAOB Independence Requirements* (product no. 006660 [paperback])

.286 Additional resources for accountants in business and industry are the Financial Reporting Alert series, designed to be used by members of an entity's financial management and audit committee to identify and understand current accounting and regulatory developments affecting the entity's financial reporting.

- Financial Reporting Alert *Current Economic Crisis: Accounting Issues and Risks for Financial Management and Reporting—2009* (product no. 0292009 [paperback])
- Financial Reporting Alert *Not-for-Profit Entities: Accounting Issues and Risks—2009* (product no. 0292209 [paperback])

AICPA reSOURCE: Accounting and Auditing Literature

.287 The AICPA has created your core accounting and auditing library online. AICPA reSOURCE is now customizable to suit your preferences or your firm's needs. Or, you can sign up for access to the entire library. Get access—anytime, anywhere—to the FASB ASC, AICPA's latest *Professional Standards*, *Technical Practice Aids*, Audit and Accounting Guides, Audit Risk Alerts, *Accounting Trends & Techniques*, and more. To subscribe to this essential online service for accounting professionals, visit www.cpa2biz.com.

AICPA Accounting Guidance Library

.288 AICPA reSOURCE Online now offers FASB ASC. As discussed previously in this alert, FASB ASC significantly changes the structure and hierarchy of accounting and reporting standards into a topically organized format.

.289 In this extraordinary member value, the AICPA is offering online access to FASB ASC along with our most popular Audit and Accounting Guides for only $659 for a one-year subscription (product number WGC-XX).

.290 This new library gives you online access to FASB ASC and the following AICPA Audit and Accounting Guides:

- *Construction Contractors*
- *Depository and Lending Institutions*

- *Employee Benefit Plans*
- *Investment Companies*
- *Life and Health Insurance Entities*
- *Not-for-Profit Entities*
- *Property and Liability Insurance Entities*

.291 The guides have been fully conformed and linked to FASB ASC and will help ease your transition to the new structure. In addition, these guides provide a key entry point to understanding the impact of FASB ASC on your work.

.292 While working in FASB ASC on AICPA reSOURCE Online, you will be able to do the following:

- Perform a full-text search
- Browse by topic
- Utilize quick go-to navigation to find a specific FASB ASC reference
- Access a cross reference report that identifies where legacy material is now located and link directly to that content
- View the source of the codified content
- Join sections and subsections
- Access an archive function of previous versions of FASB ASC content
- See all FASB ASC content that links to a given paragraph

.293 Subscribe today and make the transition to the new FASB ASC at a member-only value price of $659. Discounted multi-user subscriptions are available for this library. To order, call 888-777-7077 or go to www.cpa2biz.com.

CPE

.294 The AICPA offers a number of CPE courses that are valuable to CPAs working in public practice and industry, including the following:

- *AICPA's Annual Accounting and Auditing Update Workshop (2009–2010 Edition)* (product no. 736185 [text] or 187193 [DVD]). Whether you are in industry or public practice, this course keeps you current and informed and shows you how to apply the most recent standards.
- *SEC Reporting* (product no. 736776 [text] or 186757 [DVD]). Confidently comply with the latest SEC reporting requirements with this comprehensive course. It clarifies new, difficult, and important reporting and disclosure requirements and gives you examples and tips for ensuring compliance.
- *International Versus U.S. Accounting: What in the World is the Difference?* (product no. 731667 [text]). Understanding the differences between IFRS and U.S. GAAP is becoming more important for businesses of all sizes. This course outlines the major differences between IFRS and U.S. GAAP.

- *The International Financial Reporting Standards: An Overview* (product no. 157220 [online] or 739750HS [CD-ROM]). This course captures a live presentation on IFRSs given to the AICPA board of directors.

.295 Visit www.cpa2biz.com for a complete list of CPE courses.

Online CPE

.296 AICPA CPExpress, offered exclusively through CPA2Biz, is the AICPA's flagship online learning product. AICPA members pay $180 for a new subscription and $149 for the annual renewal. Nonmembers pay $435 for a new subscription and $375 for the annual renewal. Divided into 1-credit and 2-credit courses that are available 24 hours a day, 7 days a week, AICPA CPExpress offers hundreds of hours of learning in a wide variety of topics.

.297 To register or learn more, visit www.cpa2biz.com.

Webcasts

.298 Stay plugged in to what is happening and earn CPE credit right from your desktop. AICPA webcasts are high quality, two-hour CPE programs that bring you the latest topics from the profession's leading experts. Broadcast live, they allow you to interact with the presenters and join in the discussion. If you cannot make the live event, each webcast is archived and available on CD-ROM.

CFO Quarterly Roundtable Series

.299 The CFO Quarterly Roundtable Series, brought to you each calendar quarter via webcast, covers a broad array of "hot topics" that successful organizations employ and subjects that are important to the CFO's personal success. From financial reporting, budgeting, and forecasting to asset management and operations, the roundtable helps CFOs, treasurers, controllers, and other financial executives excel in their demanding roles.

SEC Quarterly Update Series

.300 The SEC Quarterly Update Webcast Series, brought to you each calendar quarter, showcases the profession's leading experts on what is "hot" at the SEC. From corporate accounting reform legislation and new regulatory initiatives to accounting and reporting requirements and corporate finance activities, these hard-hitting sessions will keep you "plugged in" to what is important. A must for preparers in public companies and practitioners who have public company clients, this is the place to be when it comes to knowing about the areas of current interest at the SEC.

IFRS Quarterly Webcast Series

.301 The IFRS Quarterly Webcast Series, brought to you each calendar quarter, is part of a multistep educational process to get practitioners, financial managers, and auditors up to speed on all aspects of IFRSs implementation. Over the course of the quarterly series, IFRSs will be covered in depth. International harmonization is quickly approaching, and this series will help both accountants and auditors stay abreast of the developments and changes they will need to implement.

Member Service Center

.302 To order AICPA products, receive information about AICPA activities, and get help with your membership questions, call the AICPA Service Operations Center at (888) 777-7077.

Hotlines

Accounting and Auditing Technical Hotline

.303 Do you have a complex technical question about GAAP, other comprehensive bases of accounting, or other technical matters? If so, use the AICPA's Accounting and Auditing Technical Hotline. AICPA staff will research your question and call you back with the answer. The hotline is available from 9 a.m. to 8 p.m. EST on weekdays. You can reach the Technical Hotline at (877) 242-7212 or online at www.aicpa.org/Professional+Resources/Accounting+and+Auditing/Accounting+and+Auditing+Technical+Help/.

Ethics Hotline

.304 In addition to the Technical Hotline, the AICPA also offers an Ethics Hotline. Members of the AICPA's Professional Ethics Team answer inquiries concerning independence and other behavioral issues related to the application of the AICPA Code of Professional Conduct. You can reach the Ethics Hotline at (888) 777-7077 or by e-mail at ethics@aicpa.org.

Industry Conference

.305 The AICPA offers an annual health care industry conference in the fall. The National Healthcare Industry conference is a three-day conference designed to update attendees on recent developments related to the health care industry. This conference is an unparalleled opportunity to gain the information and techniques you need to know to stay on top of trends to benefit your practice and your client offerings. With access to some of the nation's top health care specialists, you'll get up-to-the-minute information on the latest developments in health care issues. For further information about the conference, call (888) 777-7077 or visit www.cpa2biz.com.

AICPA GAQC

.306 The GAQC is a firm-based, voluntary membership center designed to improve the quality and value of governmental audits provided to purchasers of governmental audit services. Governmental audits are audits and attestation engagements of federal, state, or local governments; not-for-profit organizations; and certain for-profit organizations, such as housing projects and colleges and universities that participate in governmental programs or receive governmental financial assistance. The GAQC keeps member firms informed about the latest developments and provides them with tools and information to help them better manage their audit practice. Firms that join demonstrate their commitment to audit quality by agreeing to adhere to certain membership requirements.

.307 The GAQC has been in existence since September 2004. Since its launch, center membership has grown to almost 1200 firms from 50 states, the District of Columbia, Puerto Rico, and the U.S. Virgin Islands. The membership accounts for approximately 83 percent of the total federal expenditures covered in single audits performed by CPA firms in the Federal Audit Clearinghouse database (http://harvester.census.gov/sac/) for the year 2006 (the latest year with complete submission data).

.308 The GAQC's focus is to promote the highest quality audits and to save firms time by providing a centralized place to find information that they need, when they need it, to maximize quality and practice success. Center resources include the following:

- E-mail alerts with the latest audit and regulatory developments, including information on the Recovery Act and its impact on your audits
- Exclusive webcasts and teleconferences on compliance auditing and timely topics relevant to governmental and not-for-profit financial statement audits (optional CPE is available for a small fee, and events are archived online.)
- Dedicated GAQC Web site at http://gaqc.aicpa.org with resources, community, events, products, and a complete listing of GAQC member firms in each state
- Online member discussion forums for sharing best practices and discussing issues firms are facing
- Savings on professional liability insurance

.309 For more information about the GAQC, visit http://gaqc.aicpa.org.

The CAQ

.310 The CAQ, which is affiliated with the AICPA, was created to serve investors, public company auditors, and the markets. The CAQ's mission is to foster confidence in the audit process and aid investors and the capital markets by advancing constructive suggestions for change rooted in the profession's core values of integrity, objectivity, honesty, and trust.

.311 To accomplish this mission, the CAQ works to make public company audits even more reliable and relevant for investors in a time of growing financial complexity and market globalization. The CAQ also undertakes research, offers recommendations to enhance investor confidence and the vitality of the capital markets, issues technical support for public company auditing professionals, and helps facilitate the public discussion about modernizing business reporting. The CAQ is a voluntary membership center that provides education, communication, representation, and other means to member firms that audit or are interested in auditing public companies. To learn more about the CAQ, visit http://thecaq.aicpa.org.

AICPA Industry Expert Panel—Health Care

.312 For information about the activities of the AICPA Health Care Industry Expert Panel, visit the panel's Web page at www.aicpa.org/Professional+Resources/Accounting+and+Auditing/Accounting+Standards/expertpanel_healthcare.htm.

Industry Web Sites

.313 The Internet covers a vast amount of information that may be valuable to auditors of health care entities, including current industry trends and developments. Some of the more relevant sites for auditors with health care industry clients include those shown in the following table:

Organization	***Web Site***
Healthcare Financial Management Association	www.hfma.org
The Catholic Health Association of the United States	www.chausa.org
Federation of American Hospitals	http://www.fah.org
Centers for Medicare and Medicaid Services	www.cms.hhs.gov
U.S. Department of Health and Human Services	www.hhs.gov
Global Health Reporting	www.globalhealthreporting.org
Kaiser Family Foundation	www.kff.org
Atlantic Information Services	www.aishealth.com

.314 The health care practice areas of some of the larger CPA firms also may contain industry-specific auditing and accounting information that is helpful to auditors.

* * * *

.315 This Audit Risk Alert replaces *Health Care Industry Developments—2008*.

.316 The Audit Risk Alert *Health Care Industry Developments* is published annually. As you encounter audit or industry issues that you believe warrant discussion in next year's Audit Risk Alert, please feel free to share them with us. Any other comments that you have about the Audit Risk Alert also would be appreciated. You may e-mail these comments to ccole@aicpa.org or write to

Christopher Cole
AICPA
220 Leigh Farm Road
Durham, NC 27707-8110

.317

Appendix—Additional Web Resources

Here are some useful Web sites that may provide valuable information to accountants.

Web Site Name	*Content*	*Web Site*
AICPA	Summaries of recent auditing and other professional standards, as well as other AICPA activities	www.aicpa.org www.cpa2biz.com www.ifrs.com
AICPA Accounting Standards Executive Committee	Summaries of recently issued guides, technical questions and answers, and practice bulletins containing financial, accounting, and reporting recommendations, among other things	www.aicpa.org/Professional+Resources/Accounting+and+Auditing/Accounting+Standards
AICPA Accounting and Review Services Committee	Summaries of review and compilation standards and interpretations	www.aicpa.org/Professional+Resources/Accounting+and+Auditing/Audit+and+Attest+Standards/Accounting+and+Review+Services+Committee
AICPA Professional Issues Task Force	Summaries of practice issues that appear to present concerns for practitioners and disseminate information or guidance, as appropriate, in the form of practice alerts	www.aicpa.org/Professional+Resources/Accounting+and+Auditing/Audit+and+Attest+Standards/Professional+Issues+Task+Force
Economy.com	Source for analyses, data, forecasts, and information on the U.S. and world economies	www.economy.com
The Federal Reserve Board	Source of key interest rates	www.federalreserve.gov
Financial Accounting Standards Board (FASB)	Summaries of recent accounting pronouncements and other FASB activities	www.fasb.org

(continued)

Web Site Name	*Content*	*Web Site*
USA.gov	Portal through which all government agencies can be accessed	www.usa.gov
Government Accountability Office	Policy and guidance materials and reports on federal agency major rules	www.gao.gov
Governmental Accounting Standards Board (GASB)	Summaries of recent accounting pronouncements and other GASB activities	www.gasb.org
International Accounting Standards Board	Summaries of International Financial Reporting Standards and International Accounting Standards	www.iasb.org
International Auditing and Assurance Standards Board	Summaries of International Standards on Auditing	www.iaasb.org
International Federation of Accountants	Information on standards setting activities in the international arena	www.ifac.org
Private Company Financial Reporting Committee	Information on the initiative to further improve FASB's standard setting process to consider needs of private companies and their constituents of financial reporting	www.pcfr.org
Public Company Accounting Oversight Board (PCAOB)	Information on accounting and auditing activities of the PCAOB and other matters	www.pcaob.org
Securities and Exchange Commission (SEC)	Information on current SEC rulemaking and the Electronic Data Gathering, Analysis, and Retrieval database	www.sec.gov